

Chambal Fertilisers & Chemicals

BUY
Maintained

Near term headwinds, best bet for decontrol

Rs88

Reason for report: Q2FY12 results review

Discounting a series of adverse news flow like 1) withdrawal of shipping business de-merger plan, 2) delay in urea decontrol and likelihood of modified new pricing scheme (NPS) III with Rs350/te additional subsidy, 3) low gas availability with delay in KG D-6 ramp up plan and continuously rising re-gasified liquefied natural gas (RLNG) prices and 4) higher losses in the software business, we maintain BUY on Chambal Fertilisers & Chemicals (Chambal). Key reasons being - 1) sustained high international urea prices (US\$500/te+) and depreciating Rupee leading to increase IPP related benefits, 2) rising price disparity between DAP and urea (disparity has lately grown to 4x), which we believe, would compel the government to hike urea prices and ultimately lead to urea decontrol and 3) continued strong profitability of the trading business, which gains from decontrol of NPK. We remove decontrol benefit from FY13 earnings as it might get delayed and factor in an additional subsidy of Rs350/te as per modified NPS III. We are revising target price to Rs113/share from Rs130/share based on 11x PE FY13E base EPS.

- ▶ **Shipping de-merger withdrawal a negative.** The company withdrew the scheme for de-merging its shipping business citing unfavourable terms by lenders and other unfavourable conditions. The development is negative, as the de-merger would have spared the shareholders from the beleaguered shipping business and cleaned up the balance sheet for growth.
- ▶ **Urea decontrol may get delayed; but rationale stronger than ever.** The government has been deferring the decision to include urea under nutrient based subsidy (NBS) scheme given its adverse political fallout (with some key states going for assembly elections in near future). However, we believe, urea's overuse due to its low price compared to P&K and sustained high international urea prices would compel the government to consider the option of freeing up urea pricing.
- ▶ **Trading continues to impress.** The trading segment reported 50% jump in profitability. We believe this is sustainable as it is led by structural changes.
- ▶ **Software losses likely to be higher** at Rs700mn, primarily on account of write-offs.
- ▶ **Realign earnings, Maintain BUY.** We are adjusting our FY12-FY13 earnings as we remove benefit of decontrol from FY13 and factor in gains from additional subsidy support of 350/te. In FY12, benefit from lower interest cost, tax rate and higher trading profitability would offset impact from higher losses in software, textile and shipping.

Market Cap	Rs36.7bn/US\$748mn	Year to Mar (Consol)	2010	2011	2012E	2013E
Reuters/Bloomberg	CHMB.BO/CHMB IN	Revenue (Rs mn)	41,273	56,780	58,157	62,557
Shares Outstanding (mn)	416.2	Rec. Net Income (Rs mn)	2,505	2,406	3,612	4,283
52-week Range (Rs)	117/67	EPS (Rs)	6.0	5.8	8.7	10.3
Free Float (%)	44.9	% Chg YoY	10.6	(4.0)	50.1	18.6
FII (%)	7.0	P/E (x)	14.6	15.2	11.2	9.5
Daily Volume (US\$/'000)	6,680	CEPS (Rs)	13.7	13.5	16.3	18.0
Absolute Return 3m (%)	4.0	EV/E (x)	8.8	8.3	6.0	4.9
Absolute Return 12m (%)	2.6	Dividend Yield (%)	2.2	2.2	2.3	2.5
Sensex Return 3m (%)	(10.2)	RoCE (%)	7.4	7.0	10.0	11.2
Sensex Return 12m (%)	(16.2)	RoE (%)	18.5	16.0	21.2	21.4

Fertiliser

Target price Rs113

Earnings revision*

(%)	FY12E	FY13E
Sales	↓ 0.1	↓ 0.5
EBITDA	↓ 3.3	↓ 6.3
EPS	↑ 5.8	↓ 9.7

*Consolidated

Target price revision

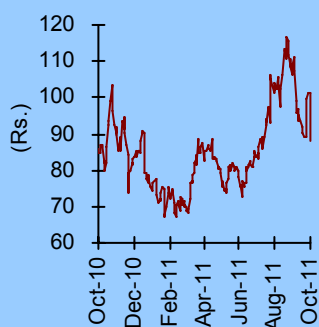
Rs113 from Rs 130

Shareholding pattern

	Dec '10	Mar '11	Jun '11
Promoters	54.9	55.1	55.1
Institutional investors	18.9	18.7	19.7
MFs and UTI	4.8	5.7	5.8
Insurance Cos.	5.7	5.7	6.2
FIs	7.8	6.7	7.0
Others	26.2	26.2	25.2

Source: NSE

Price chart



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Result analysis

Table 1: Segment-wise results analysis

(Rs mn, year ending March 31)

Results analysis	Q2FY12	Q2FY11	YoY (%)	Q1FY12	QoQ (%)
Revenues					
Urea	7,609	6,653	14.4	7,000	8.7
Shipping	984	715	37.7	889	10.7
Textile	908	801	13.3	714	27.1
Traded goods	6,881	7,181	(4.2)	2,989	130.2
	16,383	15,351	6.7	11,593	41.3
PBIT					
Urea	1,274	1,192	6.8	955	33.3
Shipping	(193)	44	(534.9)	12	(1,761.8)
Textile	(90)	86	(204.4)	(12)	671.2
Traded goods	415	278	49.3	285	45.5
	1,406	1,600	(12.2)	1,240	13.3

Source: Company data, I-Sec research

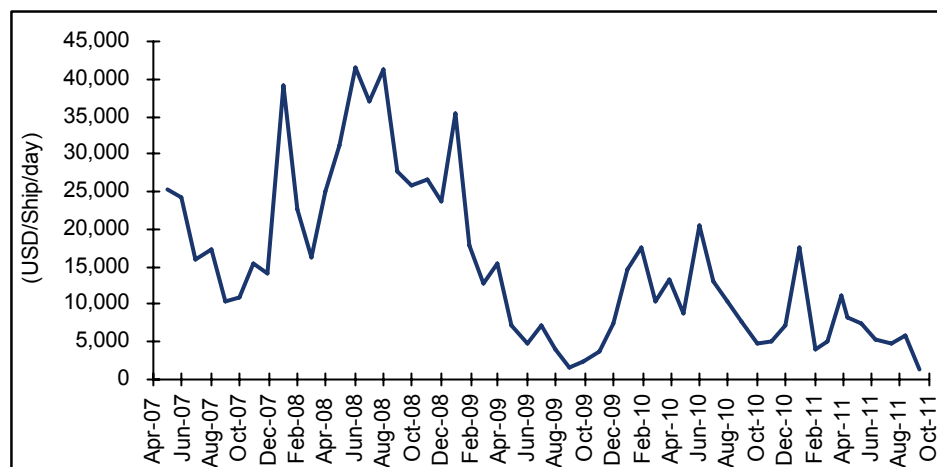
Table 2: Q2FY12 results review

(Rs mn, year ending March 31)

	Q2FY12	Q2FY11	YoY (%)	FY11	FY10	YoY (%)
Revenues	16,383	15,351	6.7	46,464	35,745	30.0
EBITDA	1,860	2,028	(8.3)	7,045	6,464	9.0
Depreciation	705	677	4.2	2,679	2,576	4.0
Other income	150	220	(31.9)	1,018	668	52.3
Interest cost	248	269	(8.0)	1,020	852	19.7
PBT	1,056	1,301	(18.8)	4,364	3,704	17.8
PAT reported	917	860	6.6	3,252	2,491	30.6
PAT adjusted	917	860	6.6	3,208	2,607	23.1

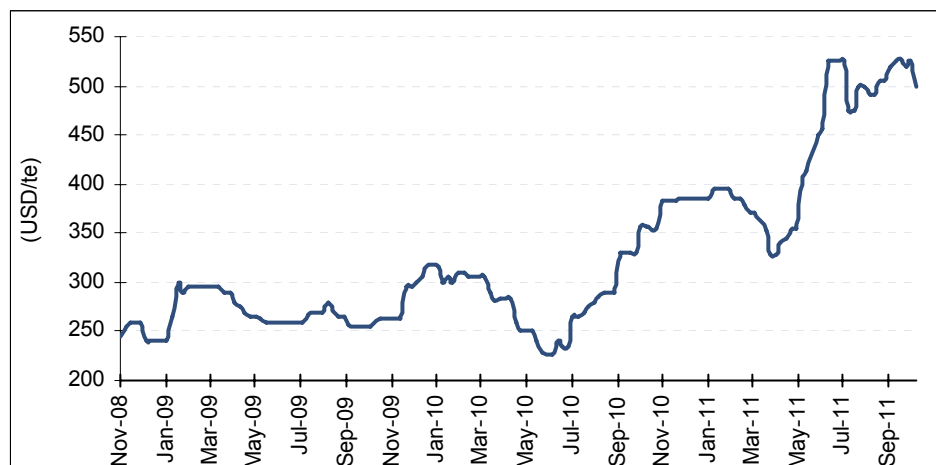
Source: Company data, I-Sec research

Chart 1: Shipping rates at their lows

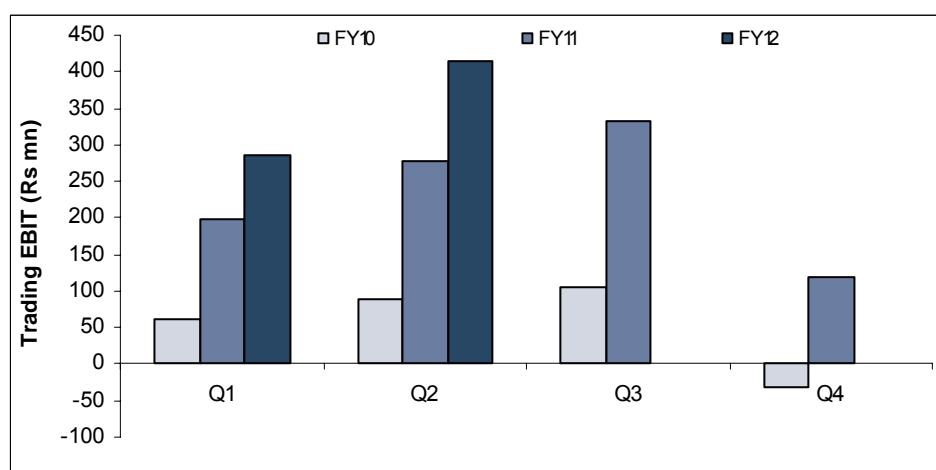


Note: Aframax rates (US\$/ship/day-average monthly rate)

Source: GE Shipping, I-Sec research

Chart 2: International urea prices sustaining at high level

Source: Bloomberg, I-Sec research

Chart 3: Bolstering trading profitability

Source: Company data. I-Sec research

Table 3: EPS sensitivity to international urea prices

UREA IPP at	US\$500/te	US\$420/te	US\$320/te
Base production (notional rated capacity)	1,845,690	1,845,690	1,845,690
Production	2,150,000	2,150,000	2,150,000
Quantity qualified for IPP	304,310	304,310	304,310
Import parity price (US\$/te)	500	420	320
85% of IPP	425	357	272
maximum IPP allowed (Min US\$250/te, max US\$425/te)	425	357	270
INR/US\$ rate	44.5	44.5	44.5
Average gas cost excluding APM(US\$/mmbtu)	9.00	9.00	9.00
Average cost for production (US\$/te)	196	196	196
Packaging & marketing cost (US\$/te)	11	11	11
PBIT (US\$/te)	218	150	63
Increase in PBIT (US\$mn)	66	46	19
IPP-linked benefit between 100% of reassessed capacity to cut-off volume (Rs mn)	63	63	
Total EBIT increase (Rs mn)	3,019	2,098	857
Impact on PAT in Rs mn	1,993	1,385	566
EPS level benefit	4.8	3.3	1.4
Incremental EPS benefit	3.4	2.0	

Source: I-Sec research

Table 4: IPP-linked benefit between 100% of reassessed capacity to cut-off volume*(Rs mn)*

Benefit till cut-off	
Volume between 100% of reassessed capacity & cut-off	116,490
Fixed cost per te	3,195
IPP at US\$320.te	14,240
Variable cost	8,056
IPP-variable cost	6,184
35% of IPP-variable cost	2,165
Bag & marketing cost	490
Current reimbursement	2,655
 Best case possible	 3195
 Benefit per te	 540
 Maximum benefit (Rs mn)	 63

Source: I-Sec Research\

Table 5: Earnings revision – Consolidated*(Rs mn)*

	FY12E			FY13E			Comment
	Old	Revised	% chg	Old	Revised	% chg	
Operating income	58,202	58,157	(0.1)	62,855	62,557	(0.5)	
EBITDA	9,301	8,996	(3.3)	10,667	9,996	(6.3)	
EPS	8.2	8.7	5.8	11.4	10.3	(9.7)	FY12: Lower tax rate and lower net interest cost offsetting higher software, textile & shipping losses FY13 : Reduced policy benefits, higher software, textile & shipping losses

Source: Company data, I-Sec Research

Table 6: Earnings revision – Standalone*(Rs mn)*

	FY12E			FY13E			Comment
	Old	Revised	% chg	Old	Revised	% chg	
Operating income	49,279	49,009	(0.5)	53,689	53,166	(1.0)	
EBITDA	8,854	8,593	(3.0)	9,919	9,393	(5.3)	
EPS	8.8	9.4	7.3	11.3	10.6	(6.4)	FY12: Lower tax rate and lower net interest cost offsetting higher textile & shipping losses FY13 : Reduced policy benefits, higher textile & shipping losses

Source: Company data, I-Sec Research

Realigning EPS estimates

Table 7: Chambal – Base case FY12 at Rs8.7/share and FY13 at Rs10.3/share

	FY12E			FY13E			Remarks
	Base case old	Rev. base case	Bull case	Base case old	Rev. base case	Bull case	
Urea business							
FY11 net of one-offs of RS210mn	3,672						FY12 urea base case US\$420/te, bull case US\$500/te FY13: urea base case US\$420/te, bull case US\$500/te. Factoring Rs350/te margin expansion in FY13 on reassessed capacity
Shipping							
FY11 net of one-offs of Rs80mn loss	7	(211)	43	7	(183)	43	Factoring US\$2000/day loss in FY13
Textile							
	100	(150)	200	150	0	250	Aligned to H1FY12 results; expecting no profit in FY13 as inventory losses occurred in FY12 should not be repeated
Trading							
	1,022	1,250	1,161	1,073	1,250	1,761	Aligning FY12 profit to H1 performance, factoring a similar profit in FY13
Total standalone EBIT	6,194	5,954	7,077	7,244	6,737	8,676	
IMACID business							
	Base case	Bull case					factoring average of old base case and bull case in FY12 & FY13
Production	300,000	330,000					
Phosphoric acid Prices	900	1000					
PBIT margin (%)	12%	15%					
US\$/INR rate	45	45					
Chambal's share in PBIT	486.0	742.5					
Shipping subsidiary							
	(25)		(25)	(25)		(25)	
Software business							
	(500)	(700)	(500)	(300)	(500)	(300)	Raised losses of software in line with revised management guidance. Reduced FY13 losses by Rs200mn
Other un-allocable income & minority	373	439	373	568	571	568	
Total	6,529	6,282	7,668	7,973	7,398	9,662	
Interest cost	1,366	1,103	1,366	986	841	986	
PBT	5,162	5,179	6,302	6,988	6,557	8,676	
Tax	1,752	1,567	2,187	2,225	2,273	2,808	
PAT	3,410	3,612	4,115	4,762	4,283	5,868	
EPS	8.2	8.7	9.9	11.4	10.3	14.1	

Source: Company data, I-Sec Research

Financial summary (consolidated)

Table 8: Profit & Loss statement

(Rs mn, year ending March 31)

	FY10	FY11	FY12E	FY13E
Operating Income (Sales)	41,273	56,780	58,157	62,557
Operating Expenses	34,241	49,985	49,161	52,561
EBITDA	7,033	6,795	8,996	9,996
<i>% margins</i>	<i>17.0%</i>	<i>12.0%</i>	<i>15.5%</i>	<i>16.0%</i>
Depreciation & Amortisation	3,189	3,229	3,185	3,201
Gross Interest	971	1,137	1,103	841
Other Income	676	1,004	359	489
Recurring PBT	3,548	3,433	5,066	6,444
Add: Extraordinaries	28	-	-	-
Less: Taxes	1,142	1,268	1,567	2,273
Minority Interest	99	241	113	113
Net Income (Reported)	2,263	2,406	3,612	4,283
Recurring Net Income	2,505	2,406	3,612	4,283

Source: Company data, I-Sec Research

Table 9: Balance sheet

(Rs mn, year ending March 31)

	FY10	FY11	FY12E	FY13E
Assets				
Total Current Assets	13,489	19,105	22,223	24,803
<i>of which cash & cash eqv.</i>	<i>2,019</i>	<i>6,164</i>	<i>9,018</i>	<i>10,550</i>
Total Current Liabilities & Provisions	6,558	7,840	8,016	8,413
Net Current Assets	6,931	11,265	14,207	16,390
Investments				
<i>of which</i>	<i>3,881</i>	<i>1,621</i>	<i>271</i>	<i>271</i>
<i>Strategic/Group</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Other Marketable</i>	<i>3,881</i>	<i>1,621</i>	<i>271</i>	<i>271</i>
Net Fixed Assets	30,602	28,198	25,863	23,511
<i>of which</i>				
<i>intangibles</i>	<i>239</i>	<i>230</i>	<i>230</i>	<i>230</i>
<i>Capital Work-in-Progress</i>	<i>488</i>	<i>731</i>	<i>731</i>	<i>731</i>
Goodwill	3,051	2,706	2,706	2,706
Total Assets	44,704	44,021	43,278	43,110
Liabilities				
Borrowings	27,412	25,803	22,303	18,803
Deferred Tax Liability	2,455	2,005	2,005	2,005
Minority Interest	478	452	565	677
Equity Share Capital	4,162	4,162	4,162	4,162
<i>Face Value per share (Rs)</i>	<i>10</i>	<i>10</i>	<i>10</i>	<i>10</i>
Reserves & Surplus*	10,172	11,560	14,205	17,424
Less: Misc. Exp.	(0)	(0)	(0)	(0)
Net Worth	14,335	15,723	18,367	21,586
Total Liabilities	44,704	44,021	43,278	43,110

*Excluding revaluation reserves

Source: Company data, I-Sec Research

Table 10: Cashflow statement

(Rs mn, year ending March 31)

	FY10	FY11	FY12E	FY13E
Operating Cashflow	4,671	3,400	6,001	6,558
Working Capital Changes	(8,693)	(188)	(89)	(650)
Capital Commitments	786	2,457	1,050	(300)
Free Cashflow	(3,237)	5,669	6,962	5,608
Cashflow from Investing Activities	676	1,004	359	489
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	1,757	(1,608)	(3,500)	(3,500)
Dividend paid	(922)	(919)	(967)	(1,064)
Extraordinary Items	28	-	-	-
Chg. in Cash & Bank balance	(2,302)	4,145	2,853	1,533

Source: Company data, I-Sec Research

Table 11: Key ratios

(Year ending March 31)

	FY10	FY11	FY12E	FY13E
Per Share Data (in Rs.)				
Diluted Recurring EPS	6.0	5.8	8.7	10.3
EPS(Basic Recurring)	6.0	5.8	8.7	10.3
Recurring Cash EPS	13.7	13.5	16.3	18.0
Dividend per share (DPS)	1.9	1.9	2.0	2.2
Book Value per share (BV)	34.4	37.8	44.1	51.9
Growth Ratios (%)				
Operating Income	(26.3)	37.6	2.4	7.6
EBITDA	4.3	(3.4)	32.4	11.1
Recurring Net Income	10.6	(4.0)	50.1	18.6
Diluted Recurring EPS	10.6	(4.0)	50.1	18.6
Diluted Recurring CEPS	12.1	(1.1)	20.6	10.1
Valuation Ratios (x)				
P/E	14.6	15.2	11.2	9.5
P/CEPS	6.4	6.5	6.0	5.4
P/BV	2.6	2.3	2.2	1.9
EV / EBITDA	8.8	8.3	6.0	4.9
EV / Operating Income	1.5	1.0	0.9	0.8
EV / Operating FCF	(15.4)	17.5	9.1	8.3
Operating Ratio (%)				
Raw Material/Sales	62.4	60.7	63.3	63.3
Other Income / PBT	27.0	41.7	9.9	11.4
Effective Tax Rate	32.2	36.9	30.9	35.3
NWC / Total Assets	11.0	11.6	12.0	13.5
Inventory Turnover (days)	39.5	44.9	43.7	43.9
Receivables (days)	57.6	44.6	43.7	43.7
Payables (days)	51.9	34.3	32.8	31.8
D/E Ratio	208.4	176.9	132.3	96.4
Return/Profitability Ratio (%)				
Recurring Net Income Margins	6.1	4.2	6.2	6.8
RoCE	7.4	7.0	10.0	11.2
RoNW	18.5	16.0	21.2	21.4
Dividend Payout Ratio	34.9	32.9	23.0	21.4
Dividend Yield	2.2	2.2	2.3	2.5
EBITDA Margins	17.0	12.0	15.5	16.0

Source: Company data, I-Sec Research

Financial summary (standalone)

Table 12: Profit & Loss statement

(Rs mn, year ending March 31)

	FY10	FY11	FY12E	FY13E
Operating Income (Sales)	35,745	46,464	49,009	53,166
Operating Expenses	29,112	39,419	40,416	43,773
EBITDA	6,633	7,045	8,593	9,393
<i>% margins</i>	<i>18.6%</i>	<i>15.2%</i>	<i>17.5%</i>	<i>17.7%</i>
Depreciation & Amortisation	2,576	2,679	2,635	2,651
Gross Interest	910	1,020	986	724
Other Income	668	1,018	373	504
Recurring PBT	3,814	4,364	5,344	6,522
Add: Extraordinaries	44	44	-	-
Less: Taxes	1,098	1,156	1,413	2,120
Minority Interest	-	-	-	-
Net Income (Reported)	2,490	3,252	3,931	4,402
Recurring Net Income	2,644	3,208	3,931	4,402

Source: Company data, I-Sec Research

Table 13: Balance sheet

(Rs mn, year ending March 31)

	FY10	FY11	FY12E	FY13E
Assets				
Total Current Assets	9,347	14,419	13,801	16,388
<i>of which cash & cash eqv.</i>	<i>300</i>	<i>2,618</i>	<i>1,736</i>	<i>3,275</i>
Total Current Liabilities & Provisions	4,011	4,403	4,579	4,977
Net Current Assets	5,336	10,015	9,222	11,412
Investments				
<i>of which</i>	<i>7,423</i>	<i>5,626</i>	<i>8,218</i>	<i>8,218</i>
<i>Strategic/Group</i>	<i>3,900</i>	<i>4,006</i>	<i>7,947</i>	<i>7,947</i>
<i>Other Marketable</i>	<i>3,523</i>	<i>1,620</i>	<i>271</i>	<i>271</i>
Net Fixed Assets	29,757	27,441	25,105	22,754
<i>of which</i>				
<i>Capital Work-in-Progress</i>	<i>437</i>	<i>658</i>	<i>658</i>	<i>658</i>
Goodwill	42	25	25	25
Total Assets	42,515	43,082	42,545	42,383
Liabilities				
Borrowings	26,160	24,837	21,337	17,837
Deferred Tax Liability	2,455	2,012	2,012	2,012
Minority Interest	-	-	-	-
Equity Share Capital	4,162	4,162	4,162	4,162
<i>Face Value per share (Rs)</i>	<i>10</i>	<i>10</i>	<i>10</i>	<i>10</i>
Reserves & Surplus*	9,738	12,071	15,034	18,372
Less: Misc. Exp. n.w.o.	-	-	-	-
Net Worth	13,900	16,233	19,196	22,534
Total Liabilities	42,515	43,082	42,545	42,383

*excluding revaluation reserves

Source: Company data, I-Sec Research

Table 14: Cashflow statement

(Rs mn, year ending March 31)

	FY10	FY11	FY12E	FY13E
Operating Cashflow	4,046	4,110	6,193	6,550
Working Capital Changes	(6,929)	(2,362)	(89)	(650)
Capital Commitments	765	1,750	(2,892)	(300)
Free Cashflow	(2,119)	3,498	3,212	5,600
Cashflow from Investing Activities	668	1,018	373	504
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	1,347	(1,323)	(3,500)	(3,500)
Dividend paid	(922)	(919)	(967)	(1,064)
Extraordinary Items	44	44	-	-
Chg. in Cash & Bank balance	(975)	2,318	(882)	1,539

Source: Company data, I-Sec Research

Table 15: Key ratios

(Year ending March 31)

	FY10	FY11	FY12E	FY13E
Per Share Data (Rs)				
Diluted Recurring EPS	6.4	7.7	9.4	10.6
EPS(Basic Recurring)	6.4	7.7	9.4	10.6
Recurring Cash EPS	12.5	14.1	15.8	16.9
Dividend per share (DPS)	1.9	1.9	2.0	2.2
Book Value per share (BV)	33.4	39.0	46.1	54.1
Growth Ratios (%)				
Operating Income	(22.2)	30.0	5.5	8.5
EBITDA	20.8	6.2	22.0	9.3
Recurring Net Income	19.7	21.3	22.5	12.0
Diluted Recurring EPS	19.7	21.3	22.5	12.0
Diluted Recurring CEPS	16.5	12.8	11.5	7.4
Valuation Ratios (x)				
P/E	13.9	11.4	10.3	9.2
P/CEPS	7.0	6.2	6.2	5.7
P/BV	2.6	2.3	2.1	1.8
EV / EBITDA	9.4	8.4	7.0	5.9
EV / Operating Income	1.7	1.3	1.2	1.0
EV / Operating FCF	(21.7)	33.7	9.8	9.3
Operating Ratio (%)				
Raw Material/Sales	64.6	64.3	69.5	69.2
Other Income / PBT				
Effective Tax Rate	25.3	31.7	9.5	11.4
NWC / Total Assets	28.8	26.5	26.4	32.5
Inventory Turnover (days)	11.8	17.2	17.6	19.2
Receivables (days)	38.5	49.2	44.9	45.1
Payables (days)	57.0	46.3	44.1	44.2
D/E Ratio	22.5	20.2	18.4	18.5
Return/Profitability Ratio (%)				
Recurring Net Income Margins	7.4	6.9	8.0	8.3
RoCE	8.0	9.2	10.9	11.5
RoNW	20.2	21.3	22.2	21.1
Dividend Payout Ratio	31.8	24.3	21.2	20.8
Dividend Yield	2.2	2.2	2.3	2.5
EBITDA Margins	18.6	15.2	17.5	17.7

Source: Company data, I-Sec Research

New I-Sec investment ratings (all ratings based on absolute return)

BUY: >15% return; ADD: 5% to 15% return; REDUCE: Negative 5% to positive 5% return; SELL: < negative 5% return

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