

Chambal Fertilisers & Chemicals

BUY
Upgrade from Hold
Rs59

Time to buy

Reason for report: Recommendation change

We upgrade Chambal Fertilisers & Chemicals to BUY from Hold with Rs75/share target price. The stock has sharply corrected in line with our view, given the disappointment over significant policy change in the urea space – Chambal has dipped 18.9% since the policy announcement in February '10, underperforming the Sensex 28%. And given the improvement in Chambal's various businesses, this correction seems a good entry point. Also, FOB urea prices have stabilised at +US\$300/te, implying ~Rs400mn upside to FY11E EBIT. Further, rising international phosphoric acid prices (to US\$650/te) augur well for the IMACID venture. Though shipping spot rate has slipped again, the broker continues to honour the time-charter at US\$25,000/day for existing ships and the management is confident of realising +US\$20,000 from the new ship, which eases our concerns. As per our best-case analysis, Chambal's FY11E EPS could be as high as Rs10.3/share vs base case of Rs7.5/share.

- ▶ **Urea prices stable at +US\$300/te; positive for Chambal.** At the current urea FOB price of US\$300/te, the companies will realise US\$275-280/te for IPP-qualifying urea capacity, higher than the base rate of US\$250/te, thus improving FY11E base-case EBIT estimate by Rs400mn.
- ▶ **Rise in phosphoric acid price can boost IMACID profitability.** Phosphoric acid price has risen to US\$650/te from a low of sub-US\$500/te. Chambal stands to gain as regards IMACID if prices rise, as is obvious from the profitability trend through FY06-08. IMACID's Q3 results had offset losses in H1FY10.
- ▶ **Shipping spot rate back to square one, but Chambal confident of realising US\$20,000/day.** Though the spot rate has fallen back to US\$8,000/day for Aframax ship, continuous honouring of the contract by the broker at US\$25,000/day for existing ships and the management's confidence on realising US\$20,000/day from new ship ease our concerns. Our base-case EBIT of Rs706mn has limited risks.
- ▶ **Upgrade to BUY; recent fall provides a good entry point.** Based on the recent underperformance by Chambal versus Sensex, all-around improvement in many of its businesses and limited downside in the shipping business (given the performance so far), we upgrade Chambal to BUY and believe that the correction is a good entry point, yielding 25% return and +3% dividend yield from a one-year perspective.

Market Cap	Rs24.6bn/US\$541mn	Year to Mar (Consol)	FY09	FY10E	FY11E	FY12E
Reuters/Bloomberg	CHMB.BO/CHMB IN	Revenue (Rs mn)	55,974	46,409	50,112	52,396
Shares Outstanding (mn)	416.2	Rec. Net Income (Rs mn)	2,162	2,685	3,105	3,259
52-week Range (Rs)	72/38	EPS (Rs)	5.2	6.5	7.5	7.8
Free Float (%)	46.8	% Chg YoY	69.9	24.2	15.6	5.0
FII (%)	6.8	P/E (x)	11.4	9.1	7.9	7.5
Daily Volume (US\$/'000)	7,270	CEPS (Rs)	12.0	14.0	15.5	15.9
Absolute Return 3m (%)	2.7	EV/E (x)	6.8	5.8	4.8	4.3
Absolute Return 12m (%)	52.0	Dividend Yield (%)	3.1	3.1	3.4	3.7
Sensex Return 3m (%)	5.5	RoCE (%)	8.5	8.8	9.7	9.9
Sensex Return 12m (%)	94.6	RoE (%)	17.5	19.3	19.6	18.1

Fertiliser

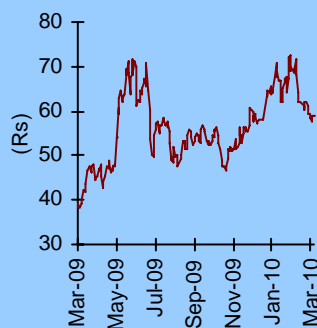
Target price Rs75

Shareholding pattern

	Jun '09	Sep '09	Dec '09
Promoters	49.6	50.3	53.2
Institutional investors	18.9	15.4	17.5
MFs and UTI	7.4	4.0	4.7
Insurance Cos.	5.5	6.2	6.0
FIs	5.9	5.2	6.8
Others	31.5	34.4	29.3

Source: NSE

Price chart


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Table 1: Chambal – FY11E bull-case EPS at +Rs10*(Rs mn, year ending March 31)*

	Assumptions		Base-case	Bull-case
Urea			4,086	4,748
Base EBIT	3,000			
Benefit of IPP at US\$250/te	1,086			
Benefit of IPP at US\$300/te	1,748			
Shipping	Base case	Bull-case	706	1,068
Double hull shipping rate	US\$25,000	US\$30,000*		
EBIT margin per ship per day	US\$10,000	US\$12,500		
4 Ship contracted at time charter till June '11				
50% profit sharing beyond US\$25,000per day				
Assumed shipping rate for fifth ship	US\$18,000	US\$30,000*		
EBIT margin per ship per day	US\$3,000	US\$15,000		
* Net realisation				
US dollar/rupee rate	45			
Textiles			100	120
Trading			300	600
Total standalone EBIT <i>(Ex dividend from IMACID)</i>			5,192	6,536
IMACID business			216	324
Production	300,000	300,000		
Phosphoric acid prices	480	600		
PBIT margin (%)	10	12		
US dollar/rupee rate	45	45		
Chambal's share in PBIT	216	324		
Shipping subsidiary			10	100
Software business			(200)	0
Other unallocable income			144	144
Total			5,362	7,104
Interest cost			821	821
PBT			4,541	6,283
Tax			1,436	1,987
PAT			3,105	4,296
EPS			7.5	10.3

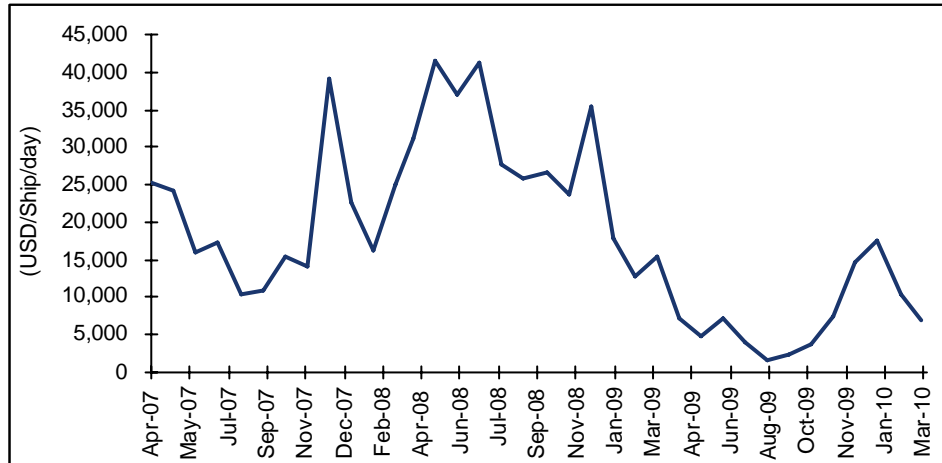
Source: Company data, I-Sec Research

Table 2: IPP-related benefit on de-bottlenecked capacity*(te)*

	FY10E	FY11E Base-case	FY11E Bull-case
Base production (notional rated capacity) (te)	1,845,690	1,845,690	1,845,690
Production (te)	2,000,000	2,140,000	2,140,000
Quantity Qualified for IPP (te)	154,310	294,310	294,310
Import parity price (US\$/te)	250	250	300
US dollar/rupee rate	46	45	45
Average gas cost excluding APM(US\$/mmbtu)	6.5	6.5	6.5
Average cost for production	168	168	168
PBIT (US\$ te)	82	82	132
Increase in PBIT (US\$mn)	12.7	24.1	38.9
Total EBIT increase (Rs mn)	582	1,086	1,748

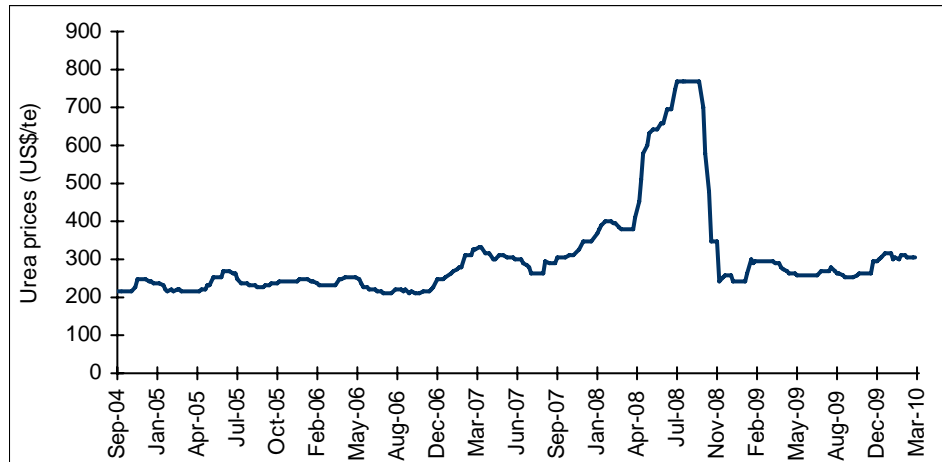
Source: Company data, I-Sec Research

Chart 1: Shipping rates back to square one



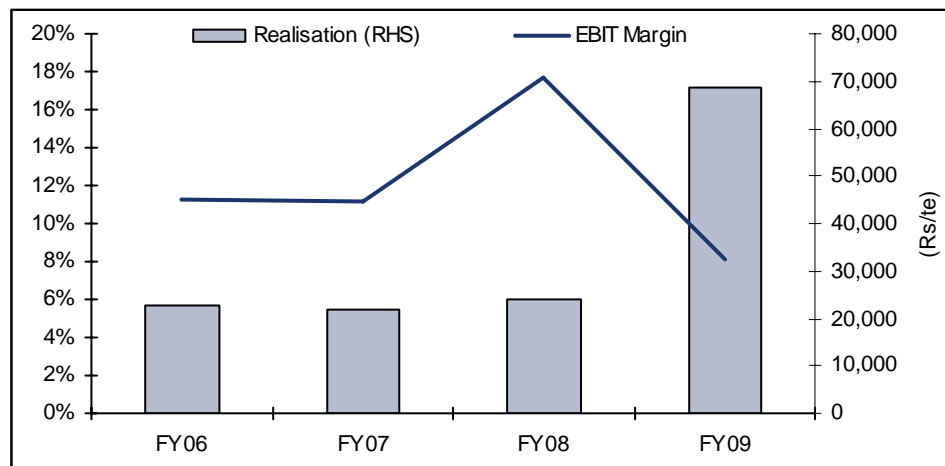
Note: Aframax rates (US\$/ship/day)
Source: GE Shipping, I-Sec Research

Chart 2: International urea prices stabilising



Source: Bloomberg, I-Sec Research

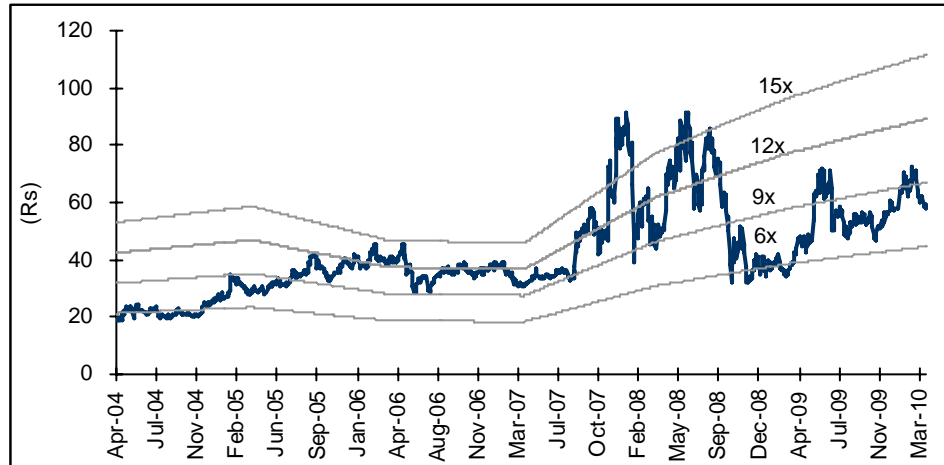
Chart 3: IMACID – Phosphoric acid realisation and profitability trend



Source: I-Sec Research

In FY09, inventory write-down was significant. Going forward, the input prices will be aligned to final Phosphoric acid prices, hence improving viability

Chart 4: Chambal P/E bands



Source: I-Sec Research

Financial Summary (Consolidated)

Table 3: Profit & Loss statement

(Rs mn, year ending March 31)

	FY09	FY10E	FY11E	FY12E
Operating Income (Sales)	55,974	46,409	50,112	52,396
Operating Expenses	49,443	39,028	41,951	44,333
EBITDA	6,531	7,381	8,161	8,063
<i>% margins</i>	<i>11.7</i>	<i>15.9</i>	<i>16.3</i>	<i>15.4</i>
Depreciation & Amortisation	2,817	3,150	3,342	3,358
Gross Interest	1,254	887	821	475
Other Income	728	639	543	532
Recurring PBT	3,189	3,983	4,541	4,762
Add: Extraordinaries	82	(44)	-	-
Less: Taxes	1,027	1,298	1,436	1,503
Net Income (Reported)	2,244	2,642	3,105	3,259
Recurring Net Income	2,162	2,685	3,105	3,259

Source: Company data, I-Sec Research

Table 4: Balance sheet

(Rs mn, year ending March 31)

	FY09	FY10E	FY11E	FY12E
Assets				
Total Current Assets	8,198	10,063	11,898	12,340
<i>of which cash & cash eqv.</i>	<i>1,309</i>	<i>1,987</i>	<i>3,417</i>	<i>3,094</i>
Total Current Liabilities & Provisions	6,112	5,508	5,963	6,204
Net Current Assets	2,085	4,555	5,935	6,136
Investments				
<i>of which</i>	<i>3,921</i>	<i>3,921</i>	<i>3,921</i>	<i>3,921</i>
<i>Strategic/Group</i>	-	-	-	-
<i>Other Marketable</i>	<i>3,921</i>	<i>3,921</i>	<i>3,921</i>	<i>3,921</i>
Net Fixed Assets	28,646	27,341	25,591	23,078
<i>of which</i>				
<i>intangibles</i>	<i>1,605</i>	<i>1,605</i>	<i>1,605</i>	<i>1,605</i>
<i>Capital Work-in-Progress</i>	<i>5,505</i>	<i>3,505</i>	<i>2,205</i>	<i>2,205</i>
Goodwill	470	470	470	470
Total Assets	36,726	37,892	37,522	35,210
Liabilities				
Borrowings	21,022	20,422	17,922	13,422
Deferred Tax Liability	2,660	2,660	2,660	2,660
Minority Interest	1	1	1	1
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*	8,895	10,660	12,791	14,978
Less: Misc. Exp. n.w.o.	14	14	14	14
Net Worth	13,043	14,808	16,939	19,127
Total Liabilities	36,726	37,892	37,522	35,210

*Excluding revaluation reserves

Source: Company data, I-Sec Research

Table 5: Cashflow statement

(Rs mn, year ending March 31)

	FY09	FY10E	FY11E	FY12E
Operating Cash flow	3,520	4,651	5,359	5,539
Working Capital Changes	1,385	(1,792)	50	(523)
Capital Commitments	(6,478)	(1,300)	(1,048)	(300)
Free Cash Flow	(1,573)	1,559	4,361	4,716
Cash flow from Investing Activities	728	639	543	532
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	1,500	(600)	(2,500)	(4,500)
Dividend paid	(876)	(876)	(974)	(1,071)
Extraordinary Items	82	(44)	-	-
Chg. in Cash & Bank balance	(139)	678	1,430	(323)

Source: Company data, I-Sec Research

Table 6: Key ratios

(Year ending March 31)

	FY09	FY10E	FY11E	FY12E
Per Share Data (in Rs.)				
Diluted Recurring EPS	5.2	6.5	7.5	7.8
EPS(Basic Recurring)	5.2	6.5	7.5	7.8
Recurring Cash EPS	12.0	14.0	15.5	15.9
Dividend per share (DPS)	1.8	1.8	2.0	2.2
Book Value per share (BV)	31.3	35.6	40.7	46.0
Growth Ratios (%)				
Operating Income	74.6	(17.1)	8.0	4.6
EBITDA	29.1	13.0	10.6	(1.2)
Recurring Net Income	69.9	24.2	15.6	5.0
Diluted Recurring EPS	69.9	24.2	15.6	5.0
Diluted Recurring CEPS	33.5	17.2	10.5	2.6
Valuation Ratios (x)				
P/E	11.4	9.1	7.9	7.5
P/CEPS	4.9	4.2	3.8	3.7
P/BV	1.9	1.7	1.4	1.3
EV / EBITDA	6.8	5.8	4.8	4.3
EV / Operating Income	0.8	0.9	0.8	0.7
EV / Operating FCF	9.0	15.0	7.2	7.0
Operating Ratio (%)				
Raw Material/Sales	69.4	59.7	59.2	59.5
SG&A/Sales				
Other Income / PBT	33.7	23.8	17.5	16.3
Effective Tax Rate	32.2	32.6	31.6	31.6
NWC / Total Assets	2.1	6.8	6.7	8.6
Inventory Turnover (days)	30.2	46.5	43.4	42.1
Receivables (days)	13.0	24.1	24.2	27.5
Payables (days)	21.8	28.1	28.0	27.4
D/E Ratio	181.6	155.9	121.5	84.1
Return/Profitability Ratio (%)				
Recurring Net Income Margins	3.9	5.8	6.2	6.2
RoCE	8.5	8.8	9.7	9.9
RoNW	17.5	19.3	19.6	18.1
Dividend Payout Ratio	33.4	28.4	26.8	28.1
Dividend Yield	3.1	3.1	3.4	3.7
EBITDA Margins	11.7	15.9	16.3	15.4

Source: Company data, I-Sec Research

Financial Summary (Standalone)

Table 7: Profit & Loss statement

(Rs mn, year ending March 31)

	FY09	FY10E	FY11E	FY12E
Operating Income (Sales)	45,960	40,766	45,099	47,383
Operating Expenses	40,568	33,802	37,605	39,987
EBITDA	5,392	6,964	7,494	7,396
% margins	11.7	17.1	16.6	15.6
Depreciation & Amortisation	2,271	2,605	2,797	2,813
Gross Interest	1,225	858	792	446
Other Income	1,190	685	638	628
Recurring PBT	3,085	4,186	4,543	4,765
Add: Extraordinaries	96	(44)	-	-
Less: Taxes	875	1,295	1,397	1,464
Net Income (Reported)	2,306	2,847	3,146	3,300
Recurring Net Income	2,210	2,891	3,146	3,300

Source: Company data, I-Sec Research

Table 8: Balance sheet

(Rs mn, year ending March 31)

	FY09	FY10E	FY11E	FY12E
Assets				
Total Current Assets	6,670	8,261	10,137	10,620
of which cash & cash eqv.	557	960	2,431	2,150
Total Current Liabilities & Provisions	5,002	4,397	4,852	5,093
Net Current Assets	1,668	3,864	5,285	5,527
Investments				
of which	6,722	7,202	7,202	7,202
Strategic/Group	2,802	3,282	3,282	3,282
Other Marketable	3,921	3,921	3,921	3,921
Net Fixed Assets	27,511	26,206	24,457	21,944
Capital Work-in-Progress	5,456	3,456	2,156	2,156
Goodwill	56	56	56	56
Total Assets	35,902	37,272	36,944	34,673
Liabilities				
Borrowings	20,436	19,836	17,336	12,836
Deferred Tax Liability	2,660	2,660	2,660	2,660
Equity Share Capital	4,162	4,162	4,162	4,162
Face Value per share (Rs)	10	10	10	10
Reserves & Surplus*	8,650	10,620	12,792	15,021
Less: Misc. Exp. n.w.o.	14	14	14	14
Net Worth	12,798	14,768	16,941	19,169
Total Liabilities	35,902	37,272	36,945	34,674

*excluding revaluation reserves

Source: Company data, I-Sec Research

Table 11: Quarterly trend

(Rs mn, year ending March 31)

	Mar-09	Jun-09	Sep-09	Dec-09
Total Revenues	8,236	7,699	9,575	11,417
% growth (YoY)	38.0	(4.4)	(44.6)	(44.6)
EBITDA	930	1,361	1,662	1,850
Margin (%)	11.3	17.7	17.4	16.2
Other income	472	205	206	126
Add: Extraordinaries	282	44	-	-
Recurring Net profit	558	509	646	797

Source: Company data, I-Sec Research

Table 9: Cashflow statement

(Rs mn, year ending March 31)

	FY09	FY10E	FY11E	FY12E
Operating Cashflow	3,107	4,811	5,305	5,485
Working Capital Changes	1,385	(1,792)	50	(523)
Capital Commitments	(6,478)	(1,780)	(1,048)	(300)
Free Cashflow	(1,986)	1,239	4,307	4,662
Cashflow from Investing Activities	1,190	685	638	628
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	1,500	(600)	(2,500)	(4,500)
Dividend paid	(876)	(876)	(974)	(1,071)
Extraordinary Items	96	(44)	-	-
Chg. in Cash & Bank balance	(77)	403	1,471	(281)

Source: Company data, I-Sec Research

Table 10: Key ratios

(Year ending March 31)

	FY09	FY10E	FY11E	FY12E
Per Share Data (Rs)				
Diluted Recurring EPS	5.3	6.9	7.6	7.9
EPS(Basic Recurring)	5.3	6.9	7.6	7.9
Recurring Cash EPS	10.8	13.2	14.3	14.7
Dividend per share (DPS)	1.8	1.8	2.0	2.2
Book Value per share (BV)	30.7	35.5	40.7	46.1
Growth Ratios (%)				
Operating Income	69.0	(11.3)	10.6	5.1
EBITDA	21.9	29.2	7.6	(1.3)
Recurring Net Income	67.2	30.8	8.8	4.9
Diluted Recurring EPS	67.2	30.8	8.8	4.9
Diluted Recurring CEPS	41.3	22.6	8.1	2.9
Valuation Ratios (x)				
P/E	11.1	8.5	7.8	7.4
P/CEPS	5.5	4.5	4.1	4.0
P/BV	1.9	1.7	1.4	1.3
EV / EBITDA	8.2	6.2	5.3	4.8
EV / Operating Income	1.0	1.1	0.9	0.7
EV / Operating FCF	9.9	14.4	7.4	7.1
Operating Ratio (%)				
Raw Material/Sales	70.9	61.6	61.9	62.1
SG&A/Sales				
Other Income / PBT	53.8	23.7	20.3	19.0
Effective Tax Rate	28.4	30.9	30.7	30.7
NWC / Total Assets	3.1	7.8	7.7	9.7
Inventory Turnover (days)	34.3	49.1	44.1	42.7
Receivables (days)	11.2	22.3	22.2	25.9
Payables (days)	16.6	19.0	18.8	18.8
D/E Ratio	180.5	152.3	118.0	80.8
Return/Profitability Ratio (%)				
Recurring Net Income Margins	4.8	7.1	7.0	7.0
RoCE	8.9	9.5	10.0	10.1
RoNW	18.3	21.0	19.8	18.3
Dividend Payout Ratio	32.5	26.3	26.5	27.7
Dividend Yield	3.1	3.1	3.4	3.7
EBITDA Margins	11.7	17.1	16.6	15.6

Source: Company data, I-Sec Research

I-Sec investment ratings (all ratings relative to Sensex over next 12 months)

BUY: +10% outperformance; **HOLD:** -10% to +10% relative performance; **SELL:** +10% underperformance

ANALYST CERTIFICATION

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