

Asian Paints-4Q06 Results Review

Strong growth

MARKET PERFORMER

Asian Paints (APL) has exhibited strong sales growth for the 4QFY06. On a consolidated basis, net sales for the quarter grew by 21%, operating profit by 30% and net profit by 27%. The operating margin also improved by 80 bps from 11.2% to 12.0%. Asian Paints Industrial Coatings, a 100% subsidiary of APL has commenced commercial production at Baddi. This company will be eligible for excise and income tax benefits and is likely to improve the domestic performance of APL.

Strong top line growth

- On a consolidated basis, APL has reported 21% YoY growth in sales for 4QFY06 from Rs. 6.31 billion to Rs. 7.65 billion compared to industry growth of around 12% during the year. All the business units witnessed good volume growth during the quarter.

Healthy domestic growth

- The 4QFY06 consolidated sales break up is shown in the following table:

Table1: Consolidated sales break up

PARTICULARS	4QFY06	4QFY05	% CHANGE	4QFY06	4QFY05
APL-Paints	5371	4272	25.7	70.2%	67.7%
Chemicals	211	216	-2.3	2.8%	3.4%
APPG(50%)+APICL	439	371	18.3	5.7%	5.9%
International	1629	1448	12.5	21.3%	23.0%
Total	7650	6307	21.3		

APL's domestic paint business grew by 26% during the quarter whereas the sales of chemicals business comprising of Phthalic Anhydride (PAN) and Pentaerythritol declined by 2%. Asian PPG and Industrial Coatings business grew by 18%. The International business grew at 13% during the quarter. The share of International business declined from 23% to 21% during the quarter.

Operating Margin Improved

- APL's operating profit grew by 30% from Rs. 707 million to Rs. 921 million. The operating margin improved by 80 bps from 11.2% to 12.0% mainly due to the decline in material cost and personnel expenses.
- Despite the sharp rise in crude oil prices, APL was able to bring down the material cost by 100 bps from 60.0% to 59.0% of net sales due to the softer prices of vegetable oils and monomers during the quarter. However, the price of crude based solvents went up during the quarter. Personnel expenses declined by 140 bps from 8.2% to 6.8% of net sales due to strong sales growth. Other expenses increased by 160 bps from 20.5% to 22.1% of net sales due to higher cost of subsidiaries.

Table 2: Quarterly Results-Consolidated

PARTICULARS	4QFY06	4QFY05	%	YEAR	ENDED	%
(in Rs. million)	MAR.06	MAR.05	CHANGE	MAR.06	MAR.05	CHANGE
Net Sales	7650	6307	21.3	30210	25739	17.4
Total Expenses	6729	5600	20.2	26293	22388	17.4
as % of Net Sales	88.0%	88.8%		87.0%	87.0%	
Raw & Pkg Materials	3741	3817	-2.0	18034	15589	15.7
(Inc.)/Dec. in stock	775	-30	NA	-113	-562	NA
Personnel Expenses	520	517	0.6	2233	2016	10.8
Other Expenses	1693	1296	30.6	6139	5346	14.8
as % of Net Sales	22.1%	20.5%		20.3%	20.8%	
Operating Profit	921	707	30.2	3917	3351	16.9
as % of Net Sales	12.0%	11.2%		13.0%	13.0%	
Other Income	117	58	101.7	320	324	-1.1
EBIDTA	1038	765	35.6	4237	3675	15.3
as % of Net Sales	13.6%	12.1%		14.0%	14.3%	
Interest	23	17	35.3	114	108	5.4
Depreciation	175	144	21.5	606	614	-1.2
Profit from associate co.	-4	0	-1528.6	-9	2	-502.3
Amor. of goodwill	28	26	7.7	76	77	-1.4
PBT	808	579	39.7	3432	2878	19.2
as % of Net Sales	10.6%	9.2%		11.4%	11.2%	
Prov. for Tax-current & deferred	353	182	94.0	1323.00	1061	24.7
as % of PBT	43.7%	31.5%		38.5%	36.9%	
PAT	455	397	14.7	2109	1817	16.1
Prior period adjustments(net)	2	-1	-300.0	-11	-5	120.9
PAT after prior adjustments	457	396	15.5	2098	1813	15.8
Minority interest	-9	29	-131.0	-23	72	-132.1
Profit after minority interest	466	367	27.1	2121	1741	21.8
Equity Capital	959	959	0.0	959	959	0.0
EPS Rs. (annualised)	19.4	15.3	27.1	22.1	18.1	21.8

- APL's other income jumped by 102% from Rs. 58 million to Rs.117 million due to higher treasury income and higher dividend income.

Rise in Interest & Depreciation

- The company's interest cost increased by 35% from Rs. 17 million to Rs. 23 million due to the increase in working capital. However, in terms of absolute values this is not significant. Depreciation was up by 22% from Rs. 144 million to Rs. 175 million.

Improvement in Net Profit

- On a consolidated basis, APL's net profit grew by 27% from Rs. 367 to Rs. 466 million during the quarter, due to the improvement in operating margin and the rise in other income.

Good overall performance

- **On a consolidated basis**, APL has reported 17% growth in net sales for FY06 from Rs. 25.74 billion to Rs. 30.21 billion. Operating profit was up by 17% from Rs. 3.35 billion to Rs. 3.92 billion. APL's operating margin was maintained at 13.0%. The company's net profit for the year grew by 22% from Rs. 1.74 billion to Rs. 2.12 billion.

Other Developments

- APL has achieved excellent growth in all wall finish products in FY06. The company has 7000 Colour Worlds installed in the country and has penetrated into small towns.
- The company has increased the prices of decorative paints in June and Nov'05 to compensate for the increase in raw material cost and to maintain the operating margin.
- APL has nationwide launched Apex Ultima. It has introduced Utsav economy range of products during the year.
- Asian Paints Home Solutions has now presence in 10 cities.
- **Sales of Asian PPG increased by 18% to Rs. 2.80 billion during FY06. APICL powder coating sales was up by 36% to Rs. 390 million during the year.**
- APL has increased the capacity of Sriperumbudur plant to 50,000 KL/ annum. The 1400 KL Baddi plant went on stream in April '06. The Baddi plant will be eligible for excise and income tax benefits.
- The protective coatings, road marking and floor coating segment grew by over 20% due to good growth in protective coating segment.

International operations

- APL's paint value sales increased by 15.7% to Rs. 5.3 billion. Operating margins were under pressure as material cost increase was significant.
- The International business unit reported higher loss of Rs. 99.7 million against Rs. 39 million loss in FY05. This was attributed to the higher share of loss from associate company in Philippines and subsidiaries in China, Malaysia, Thailand, Bangladesh and Sri Lanka.
- The performance of Middle East, Caribbean and South Pacific regions was good during FY06. South Asia and South East Asia have under performed.
- The region wise EBIDTA is indicated in the following table:

Table 3: Region wise EBIDTA

REGION (\$'000)	2005	2004	% CHANGE
Middle East	3273	2267	44.4
Caribbean	2493	2487	0.2
South Pacific	1218	1256	-3.0
South East Asia	-3209	918	NA
South Asia	-304	18	NA
Total	3471	6946	-50.0

The region wise EBIDTA indicate that the South East Asia and South Asia regions have reported losses in 2005. There was a drop of \$ 3.47 million (Rs. 154 million) in EBIDTA.

Concerns

- **APL has provided Rs. 336 million as diminution in value of international investments during 4QFY06 due to the erosion in net worth of certain subsidiaries in South East Asia and South Asia.**
- The increase in interest rates is likely to slow down the demand in the auto and housing sectors. The interest rates have already gone up by 50-100 bps in last 6 months. Any further increase in the interest rate will be detrimental to the growth in the auto and housing sectors.
- The sharp increase in the crude oil prices is likely to increase the input cost as majority of solvents and chemicals are derived from crude oil. The manufacturers will have no choice but to pass on the increase in raw material price to the consumers.
- The increase in the prices of petrol and diesel are likely to reduce the consumption. This is likely to adversely affect the future demand in the auto sector.

Financials

- During FY06, the company has invested Rs. 543 million towards capital expenditure. APL has plans to spend Rs. 1.5 billion on capex in FY07.
- On a consolidated basis, we expect APL to report 16% growth in net sales and 18% growth in net profit over next 2 years. We expect the operating margin to improve from 13.0% in FY06 to 13.3% in FY07 and further improve to 13.5% in FY08.
- The CMP of Rs. 570 discounts the FY07E EPS of Rs. 25.9 by 22.0x and FY08E EPS of Rs. 31.0 by 18.4x. We expect the scrip to be **Market performer**.

Income Statement-Consolidated

Particulars	FY04A	FY05A	FY06A/E	FY07E	FY08E
(in Rs. Million)					
Net sales	22179	25605	30210	35060	40332
Operating expenses	19208	22254	26293	30413	34892
Operating profit	2972	3351	3917	4647	5439
Other income	264	324	320	330	350
EBIDTA	3235	3675	4237	4977	5789
Depreciation	628	614	606	700	740
Interest	152	108	114	100	80
PBT	2416	2878	3432	4097	4895
Tax-current+deferred	941	1061	1323	1620	1932
Net profit	1449	1741	2121	2483	2974
EPS Rs.	15.1	18.1	22.1	25.9	31.0

Source: Company, HDFC Sec. Estimates

Balance Sheet-Consolidated

Particulars	FY04A	FY05A	FY06A/E	FY07E	FY08E
(in Rs. Million)					
Share Capital	959	959	959	959	959
Reserves & Surplus	4336	4713	5436	6681	8299
Total Debt	1693	2395	2000	2100	1550
Deferred tax	533	353	328	298	260
Minority Interest	698	639	610	590	570
Capital Employed	8219	9059	9334	10628	11639
Net Block	4694	4273	4203	5103	5063
Capital WIP	46	97	65	70	80
Investments	1018	1138	1250	1400	1800
Current assets, loans & adv.	7476	9077	10666	11825	13416
Less: Current Liabilities & Prov.	5720	6178	7450	8320	9300
Goodwill on consolidation	582	500	420	340	340
Retirement benefits assets	124	152	180	210	240
Capital Deployed	8219	9059	9334	10628	11639

Source: Company, HDFC Sec. Estimates

Ratio

Particulars	FY04A	FY05A	FY06A/E	FY07E	FY08E
Revenue Growth (%)	28.2%	15.4%	18.0%	16.1%	15.0%
Operating margin (%)	13.4%	13.1%	13.0%	13.3%	13.5%
EBIDTA margin (%)	14.6%	14.4%	14.0%	14.2%	14.4%
Net margin (%)	6.5%	6.8%	7.0%	7.1%	7.4%
P/E (x)	37.7	31.4	25.8	22.0	18.4
ROCE (%)	19.5%	20.4%	23.9%	24.3%	26.2%
RONW (%)	27.4%	30.7%	33.2%	32.5%	32.1%
EV/EBIDTA	17.4	15.5	13.4	11.4	9.7
Book Value	55.2	59.1	66.7	79.6	96.5
P/BV (x)	10.3	9.6	8.5	7.2	5.9
EPS growth (%)	4.1%	20.2%	21.9%	17.0%	19.8%

Source: Company, HDFC Sec. Estimates

Cash Flow

Particulars	FY04A	FY05A	FY06A/E	FY07E	FY08E
(in Rs. Million)					
PBT	2416	2878	3432	4097	4895
Less: current Tax	854	957	1348	1650	1970
Add: depreciation	707	691	682	775	814
Add: interest exp.	152	108	114	100	80
Changes in WC	207	-1444	-1693	-1195	-1630
Operating cash flow	2488	1067	2613	2612	2727
Change in debt	-276	723	-395	100	-550
Dividend	-895	-1032	-1373	-1208	-1318
Financing cash flow	-1339	-418	-1882	-1208	-1948
Investing cash flow	-1131	-739	-503	-1604	-709
Total cash flow	18	-90	227	-200	70
Opening balance	680	698	608	836	635
Closing balance	698	608	836	635	706

Source: Company, HDFC Sec. Estimates

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