



## Asian Paints

STOCK INFO.	BLOOMBERG
BSE SENSEX: 14,516	APNT IN
	REUTERS CODE
S&P CNX: 4,215	ASPN.BO

5 February 2007

Buy

Previous Recommendation: Buy

Rs780

Equity Shares (m)	95.9
52-Week Range	835/501
1,6,12 Rel. Perf. (%)	-1/-7/-35
M.Cap. (Rs b)	74.8
M.Cap. (US\$ b)	1.7

YEAR	NET SALES	Adj.PAT	EPS	EPS	P/E	P/BV	ROE	ROCE	EV/	EV/
END	(RS M)	(RS M)	(RS)	GROWTH (%)	(X)	(X)	(%)	(%)	SALES	EBITDA
3/06A	23,192	2,214	23.1	25.6	33.8	11.8	35.0	44.5	3.1	20.5
3/07E	27,830	2,674	27.9	20.8	28.0	9.9	35.5	50.6	2.6	16.9
3/08E	32,283	3,221	33.6	20.5	23.2	8.1	34.9	50.4	2.2	13.9

- Asian Paints' 3QFY07 standalone revenue growth has been below our estimates owing to an early Diwali, whereby most of the festive sales came in the September quarter. Standalone net sales for 3QFY07 grew 12.9% YoY to Rs7.06b v/s our estimate of Rs7.4b
- EBITDA margins declined 125bp during the quarter on a YoY basis to 14.3% mainly due to 70bp increase in raw material prices.
- Asian Paints has opted for a 3.5% price increase in decorative paints in the last nine months including the most recent hike, by 1.3%, on 17 January 2007.
- Consolidated revenues grew by 17% to Rs.9.4b while net profit grew by 14% to Rs713.9m. Higher growth was on account of a 30% growth in international business driven primarily by the Middle-East market.
- We expect margin pressure to ease going forward with the prices of key raw materials such as titanium dioxide and crude-based inputs, softening. Volume growth continues to be strong given the rising disposable income and construction boom.
- We expect the company to maintain valuation premium due to strong growth prospects, strong brands and excellent track record of rewarding shareholders. The stock is trading at 28x FY07E EPS and 23.2x FY08E EPS. We maintain **Buy**.

### QUARTERLY PERFORMANCE

(Rs Million)

Y/E MARCH	FY06				FY07				FY06	FY07E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
<b>Net Sales</b>	<b>5,106</b>	<b>6,192</b>	<b>6,255</b>	<b>5,645</b>	<b>6,034</b>	<b>7,849</b>	<b>7,060</b>	<b>6,887</b>	<b>23,192</b>	<b>27,830</b>
Change (%)	27.1	19.6	7.9	27.7	18.2	26.8	12.9	22.0	19.5	20
Total Expenditure	4,378	5,186	5,282	4,832	5,095	6,646	6,049	4,832	19,672	23,606
<b>EBITDA</b>	<b>728</b>	<b>1,006</b>	<b>973</b>	<b>812</b>	<b>939</b>	<b>1,203</b>	<b>1,010</b>	<b>1,071</b>	<b>3,519</b>	<b>4,224</b>
Margin (%)	14.3	16.2	15.6	14.4	15.6	15.3	14.3	15.6	15.2	15.2
Change (%)	18.1	24.2	7.8	33.4	29.0	19.6	3.8	31.9	19.8	20
Interest	5.5	9	17	7	13.0	18	23	11	38	65
Depreciation	111	113	112	120	110	115	112	178	455	515
Other Income	60	71	83	145	64	101	108	128	359	401
Operational PBT	672	956	927	830	880	1,171	983	1,010	3,385	4,045
Non Recurring Items	0	-17	3	-334	0.4	-2	2	0	-346	1
<b>PBT</b>	<b>672</b>	<b>938</b>	<b>930</b>	<b>496</b>	<b>881</b>	<b>1,170</b>	<b>985</b>	<b>1,010</b>	<b>3,039</b>	<b>4,046</b>
Tax	229	326	327	310	299	401	331	383	1,192	1,415
Deferred Tax	1	0	-6	-16	1	-7	0	-39	-21	-45.0
Effective Tax Rate (%)	34	34.8	34.4	59.1	34	33.7	33.7	34.0	38.5	34
<b>PAT</b>	<b>442</b>	<b>612</b>	<b>610</b>	<b>203</b>	<b>580</b>	<b>776</b>	<b>653</b>	<b>666</b>	<b>1,868</b>	<b>2,676</b>
<b>Adjusted PAT</b>	<b>442</b>	<b>629</b>	<b>606</b>	<b>537</b>	<b>580</b>	<b>777</b>	<b>651</b>	<b>666</b>	<b>2,214</b>	<b>2,675</b>
Change (%)	32	27.9	11.4	31.3	31	23.6	7.4	24	24	20.8

E: MOST Estimates

### Asian Paints (standalone) performance below estimates

Asian Paints' standalone revenue growth has been below our estimates owing to an early Diwali, whereby the bulk of festive sales had come in the September quarter. Standalone net sales grew 12.9% YoY for 3QFY07 to Rs7.06b. Volume growth was around 2% lower than value growth, while industrial paints recorded strong growth. The company also benefited from the new powder coating plant in Baddi. In FY06, the company had commissioned a 3,500 tonne plant in Baddi for powder coating.

EBITDA margins declined 125bp YoY to 14.3% mainly due to 70bp increase in raw material prices. Adjusted PAT grew by 7% to Rs651m. Growth in consolidated revenues and profits before minority interest was higher at 16.6% to Rs.9.4b while profit before minority interest grew by 19.7% to Rs750.2m. Higher growth was on account of a 30% growth in revenues and improved profitability in the international business.

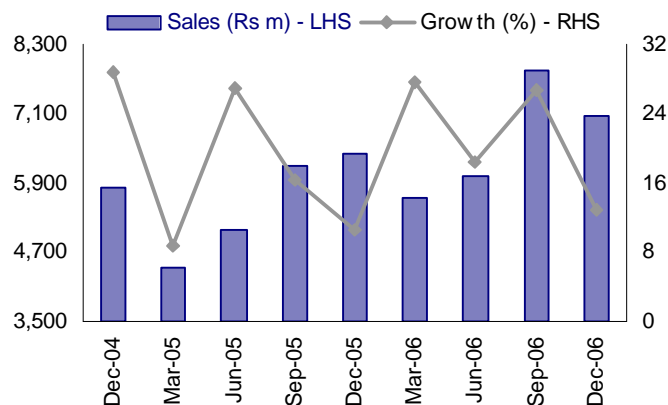
#### SEGMENTAL REVENUE (RS M)

SEGMENT REVENUE	3QFY06	3QFY07	CHG. (%)
<b>Segment Revenue</b>			
Paints	6,078.2	6,832.5	12
Others	350.4	474.6	35
<b>Segment PBIT</b>			
Paints	987.4	1,033.4	5
Others	42.4	47.3	12
<b>Margins (%)</b>			
Paints	16.2	15.1	
Others	12.1	10.0	

Source: Company

Segmental standalone paint revenues grew by 12.4% with 120bp margin decline while Pthalic Anhydride reported 35% sales growth and 210bp margin decline to 10%.

#### SALES TREND ANALYSIS



Source: Company

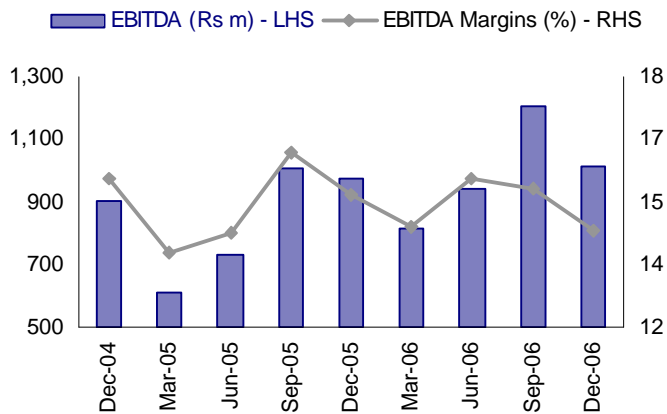
### Demand for industrial as well as decorative paints continues to be robust

Asian Paints is setting up a 15,000 tonne plant in Taloja. This plant will be the first plant exclusively for industrial coating. Further the company plans to ramp-up capacity in the emulsions plant at Sriperambudur from 30,000 KL to 50,000 KL in FY07 (the plant can be ramped up to 100,000 KL). These expansion initiatives indicate bright prospects for the industrial as well as the decorative paint segment. Repainting constitutes around 65-70% of the total painting demand whilst the remainder arises from new construction activity. Demand for repainting continues to be robust led by rising disposable incomes (4<sup>th</sup> year of 7% +GDP growth), while the construction boom will drive the demand for new painting.

### Pressure on margins likely to ease

The price of vegetable oil continues to be on an uptrend. However, management expects prices of key inputs such as titanium dioxide and crude-based materials such as PAN, pentaerythritol and MTO to turn benign. Further, with market conditions being buoyant the company has been able pass on the cost pressures. Hence, we could see margins in the coming quarter improving.

TREND IN EBITDA MARGIN



Source: Company

### International business boosts consolidated performance

Consolidated sales and PAT growth were higher at 16.6% to Rs9.35b and 14% to Rs713.9m. Higher growth in revenues was on the back of a 30% growth in the international business, which contributed 24% to sales and 13.6% to consolidated profits in 3QFY07. Growth in international business was primarily driven by the Middle

East market (contributes approximately 37% to total international revenues). The company regained pricing power and also took certain cost control and restructuring initiatives in the Middle East markets, which paid off. PAT margin in the international business was at 2%, which has been management's objective.

Longer than expected turnaround of Asian Paints' international operations has been an area of concern. While certain pockets are turning profitable, certain geographical regions, particularly the South East Asian region, continue to pull down earnings. However, there could be a possibility of the company divesting certain loss-making businesses to improve earnings contribution of overseas ventures.

### Valuation and view

We are bullish on the company in the coming quarters due to boom in the construction activity. We expect the company to maintain valuation premium due to strong growth prospects, strong brands and excellent track record in rewarding shareholders. The stock is trading at 28x FY07E EPS and 23.2x FY08E EPS. We maintain **Buy**.

## Asian Paints: an investment profile

### Company description

Asian Paints is the largest paint manufacturer and marketer in India with 45% share in the decorative paints. The company has a presence in automotive segment via a JV with PPG of the US. Asian Paints acquired Berger International of Singapore to enter the league of top ten paint companies in the world.

### Key investment arguments

- Growing investment in housing and construction will likely drive demand for decorative paints by 12%-13% over the next 3-5 years.
- New powder coating unit will boost income and profits for the high-growth industrial segment.

### Key investment risks

- High spread and geographical diversification increases execution risk.
- Raw material prices can impact profit margins due to limited pricing power as a result of presence of the unorganized sector and intense competition.

### Recent developments

- The company has commissioned a 3,500t p.a. plant in Baddi for powder coating. The unit enjoys excise and tax benefits.
- Asian Paints is setting up a 15,000t plant in Talaja. This plant will be the first exclusive industrial coating plant.

### Valuation and view

- We have an EPS forecast upward of Rs27.9 for FY07 and Rs33.6 for FY08 on a standalone basis.
- The stock is trading at 28x FY07E EPS and 23.2x FY08E its standalone EPS. We maintain **Buy**.

### Sector view

- We are positive on the sector. Volume growth remains strong although input cost pressure continues.
- Longer term prospects bright, given rising incomes, low penetration and booming construction and infrastructure development.

#### COMPARATIVE VALUATIONS

		ASIAN PAINTS	ITC	HLL
P/E (x)	FY07E	28.0	23.5	31.1
	FY08E	23.2	19.7	25.2
EV/EBITDA (x)	FY07E	16.9	15.3	26.5
	FY08E	13.9	12.7	21.2
EV/Sales (x)	FY07E	2.6	4.9	3.7
	FY08E	2.2	4.1	3.3
P/BV (x)	FY07E	9.9	6.2	18.0
	FY08E	8.1	5.4	15.6

#### SHAREHOLDING PATTERN (%)

	DEC.06	SEP.06	DEC.05
Promoter	47.8	47.8	46.8
Domestic Inst	11.8	12.6	13.4
Foreign	21.8	21.0	21.7
Others	18.6	18.6	18.1

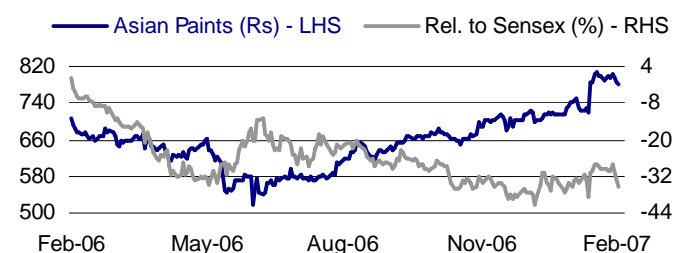
#### EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY07	27.9	27.9	-0.1
FY08	33.6	33.9	-0.9

#### TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
780	875	12.2	Buy

#### STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT (UNCONSOLIDATED)					
(Rs Million)					
Y/E MARCH	2005	2006	2007E	2008E	2009E
<b>Net Sales</b>	<b>19,415</b>	<b>23,192</b>	<b>27,830</b>	<b>32,283</b>	<b>37,125</b>
Change (%)	14.4	19.5	20.0	16.0	15.0
Raw Materials	11,154	13,517	16,308	18,885	21,644
Staff Cost	1,179	1,290	1,509	1,720	1,944
Admin. & Other Exp.	4,144	4,865	5,789	6,650	7,611
<b>EBITDA</b>	<b>2,938</b>	<b>3,519</b>	<b>4,224</b>	<b>5,027</b>	<b>5,927</b>
% of Net Sales	15.1	15.2	15.2	15.6	16.0
Depreciation	476	455	515	550	580
EBIT	2,732	3,077	4,108	4,939	5,870
Interest	28	38	65	75	80
Other Income	316	359	401	462	524
Non Recurring Exp.	46	346	1	0	0
<b>PBT</b>	<b>2,705</b>	<b>3,039</b>	<b>4,043</b>	<b>4,864</b>	<b>5,790</b>
Tax	988	1,192	1,415	1,702	1,911
Deferred Tax	-18	-21	-45	-60	-60
Rate (%)	36.5	39.2	35.0	35.0	33.0
<b>PAT</b>	<b>1,735</b>	<b>1,868</b>	<b>2,673</b>	<b>3,222</b>	<b>3,940</b>
<b>Adjusted PAT</b>	<b>1,763</b>	<b>2,214</b>	<b>2,674</b>	<b>3,221</b>	<b>3,939</b>
Change (%)	16.1	25.6	20.8	20.5	22.3

BALANCE SHEET (UNCONSOLIDATED)					
(Rs Million)					
Y/E MARCH	2005	2006	2007E	2008E	2009E
Share Capital	959	959	959	959	959
Reserves	4,763	5,373	6,570	8,260	10,559
<b>Net Worth</b>	<b>5,722</b>	<b>6,332</b>	<b>7,529</b>	<b>9,219</b>	<b>11,518</b>
Loans	840	671	670	670	670
<b>Capital Employed</b>	<b>6,561</b>	<b>7,002</b>	<b>8,199</b>	<b>9,889</b>	<b>12,188</b>
Gross Fixed Assets	7,127	8,327	8,827	9,327	9,827
Less: Depreciation	4,015	4,470	4,985	5,535	6,115
<b>Net Fixed Assets</b>	<b>3,112</b>	<b>3,857</b>	<b>3,842</b>	<b>3,792</b>	<b>3,712</b>
Capital WIP	83	83	83	83	83
Investments	2,584	2,953	3,987	5,494	6,998
<b>Curr. Assets</b>	<b>5,925</b>	<b>5,111</b>	<b>5,875</b>	<b>6,669</b>	<b>8,140</b>
Inventory	3,308	2,345	2,814	3,264	3,754
Debtors	1,490	1,639	1,966	2,281	2,623
Cash & Bank Balance	210	210	177	206	845
Loans & Advances	727	727	727	727	727
Other Current Assets	190	190	190	190	190
<b>Curr. Liabilities</b>	<b>4,838</b>	<b>4,676</b>	<b>5,218</b>	<b>5,718</b>	<b>6,254</b>
Creditors	2,787	2,625	3,167	3,667	4,203
Other Liabilities	934	934	934	934	934
Provisions	1,117	1,117	1,117	1,117	1,117
<b>Net Curr. Assets</b>	<b>1,087</b>	<b>436</b>	<b>657</b>	<b>951</b>	<b>1,886</b>
Deferred Tax Liability	-305	-326	-370	-431	-491
<b>Appl. of Funds</b>	<b>6,561</b>	<b>7,003</b>	<b>8,199</b>	<b>9,889</b>	<b>12,188</b>

E: MOST Estimates

RATIOS (UNCONSOLIDATED)					
Y/E MARCH	2005	2006	2007E	2008E	2009E
<b>Basic (Rs)</b>					
<b>EPS</b>	<b>18.4</b>	<b>23.1</b>	<b>27.9</b>	<b>33.6</b>	<b>41.1</b>
Cash EPS	34.9	416	49.7	58.8	70.4
Book Value	59.7	66.0	78.5	96.1	120.1
DPS	9.5	11.5	13.5	14.0	15.0
Payout (incl. Div. Tax.)	52.5	59.1	48.5	41.7	36.5
<b>Valuation (x)</b>					
P/E		33.8	28.0	23.2	19.0
Cash P/E		18.7	15.7	13.3	11.1
EV/EBITDA		20.5	16.9	13.9	11.4
EV/Sales		3.1	2.6	2.2	1.8
Price/Book Value		11.8	9.9	8.1	6.5
Dividend Yield (%)		15	17	18	19
<b>Profit. Ratios (%)</b>					
RoE	30.8	35.0	35.5	34.9	34.2
RoCE	42.2	44.5	50.6	50.4	48.5
<b>Turnover Ratios</b>					
Debtors (Days)	28	26	26	26	26
Inventory (Days)	62	37	37	37	37
Creditors (Days)	52	41	41	41	41
Asset Turnover (x)	3.0	3.3	3.4	3.3	3.0
<b>Leverage Ratio</b>					
Debt/Equity (x)	0.1	0.1	0.1	0.1	0.1

CASH FLOW STATEMENT					
(Rs Million)					
Y/E MARCH	2005	2006	2007E	2008E	2009E
OP/(loss) before Tax	2,462	3,064	3,709	4,477	5,347
Int./Div. Received	316	359	401	462	524
Depreciation and Amort.	476	455	515	550	580
Interest Paid	-28	-38	-65	-75	-80
Direct Taxes Paid	-988	-1,192	-1,415	-1,702	-1,911
(Incr)/Decr in WC	-485	651	-255	-264	-296
<b>CF from Operations</b>	<b>1,754</b>	<b>3,300</b>	<b>2,890</b>	<b>3,447</b>	<b>4,164</b>
Extraordinary Items	-46	-346	-1	0	0
(Incr)/Decr in FA	-659	-1,200	-500	-500	-500
(Pur)/Sale of Investments	-159	-369	-1,034	-1,507	-1,504
<b>CF from Invest.</b>	<b>-864</b>	<b>-1,915</b>	<b>-1,535</b>	<b>-2,007</b>	<b>-2,004</b>
(Incr)/Decr in Debt	135	-169	-1	0	0
Dividend Paid	-1,037	-1,258	-1,476	-1,531	-1,640
Others	-24	41	89	119	119
<b>CF from Fin. Activity</b>	<b>-926</b>	<b>-1,386</b>	<b>-1,388</b>	<b>-1,412</b>	<b>-1,521</b>
<b>Incr/Decr of Cash</b>	<b>-36</b>	<b>-1</b>	<b>-34</b>	<b>28</b>	<b>638</b>
Add: Opening Balance	246	210	210	177	206
<b>Closing Balance</b>	<b>210</b>	<b>210</b>	<b>177</b>	<b>206</b>	<b>845</b>



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**Asian Paints**

- |   |    |
|---|----|
| 1. Analyst ownership of the stock                       | No |
| 2. Group/Directors ownership of the stock               | No |
| 3. Broking relationship with company covered            | No |
| 4. Investment Banking relationship with company covered | No |

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