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Phillips Carbon Black

Black Magic

Phillips Carbon Black (PCBL), part of the RPG Group, is the leading producer of carbon black in India, with ~48% of the total installed capacity in FY2010. Currently, with ~65% of the total carbon black production in the country being consumed by the tyre industry, PCBL is well poised to benefit from the rising demand for tyres going ahead. Moreover, we expect the company's power segment to start contributing substantially to its bottom-line in FY2011 and FY2012 and provide stability to its earnings. We have valued PCBL on the sum-of-the parts valuation methodology and arrived at a Target Price of Rs270 wherein we have valued PCBIL's carbon black segment at Rs144//share (1x FY2012E P/BV) and the power segment at Rs126/share (NPV method). **We Re-initiate Coverage on the stock with a Buy recommendation.**

Volume growth backed by capacity expansions to drive carbon black revenues: To capitalise on the rising demand for tyres PCBL has been on the expansion spree. Post commissioning of the 90,000MT green-field plant at Mundra in October 2009, the company's current installed capacity stands at 360,000MT. PCBL plans to further increase its capacity to 410,000MT by setting up a brown-field plant of 50,000MT in Mundra, which is expected to be operational by 3QFY2011E. Thus, with additional capacities coming on stream, we expect volumes and revenues of the carbon black segment to register CAGR of 15.3% and 22.3% respectively over FY2010-12E.

Power segment- The game changer: PCBL currently has in place 60.5MW of power generating capacity and with further capacities coming up, the same will be enhanced to 77.5MW by 3QFY2012E. Since PCBL utilises the off-gas generated during the manufacture of carbon black for producing power, the company has no raw material requirements. Hence, although the power revenues would contribute a mere ~7% to the company's total top-line in FY2012E, on the bottom-line front it would contribute ~50% of total profit. Thus, a high proportion of the power revenues would percolate to the bottom-line and lend stability to the company's earnings while significantly de-risking its business model.

Key Financials

Y/E March (Rs cr)	FY2009	FY2010	FY2011E	FY2012E
Net Sales	1,163	1,235	1,643	1,899
% chg	*12.6*	*6.0*	*33.3*	*15.6*
Net Profit	(72.1)	122.7	143.9	175.4
% chg	-	-	*17.2*	*22.0*
EBITDA Margin (%)	-	15.4	16.1	16.2
EPS (Rs)	-	43.4	41.7	50.9
P/E (x)	-	4.9	5.1	4.2
P/BV (x)	2.7	1.8	1.3	1.0
RoE (%)	-	44.8	31.7	26.6
RoCE (%)	-	20.7	22.8	23.6
EV / Sales (x)	1.0	1.0	0.6	0.5
EV/EBITDA (x)	-	6.5	4.0	3.0

Source: Company, Angel Research

BUY

CMP	Rs213
Target Price	Rs270
Investment Period	12 Months

Stock Info	
Sector	Carbon Black
Market Cap (Rs cr)	707
Beta	0.8
52 Week High / Low	229/134
Avg. Daily Volume	51760
Face Value (Rs)	10
BSE Sensex	18,221
Nifty	5,479
Reuters Code	PHIL.BO
Bloomberg Code	PHCB@IN

Shareholding Pattern (%)	
Promoters	45.8
MF / Banks / Indian FIs	25.7
FII / NRIs / OCBs	14.6
Indian Public / Others	13.9

Abs. (%)	3m	1yr	3yr
Sensex	7.0	18.3	18.2
Phillips Carbon	15.9	50.8	27.8

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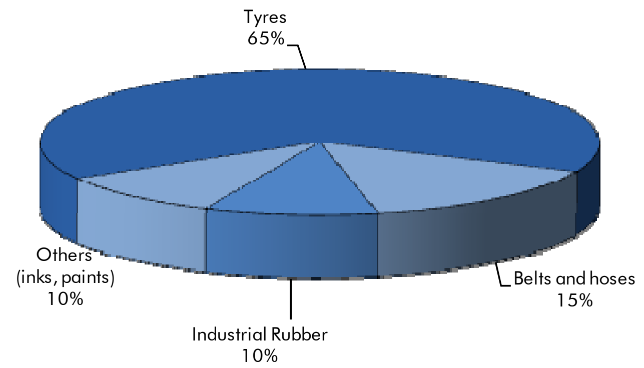
Industry Overview

Carbon black, a fluffy black powdery substance, is one of the key raw materials used in the manufacture of tyres, as it imparts high resistance to abrasion, longevity and grip. Carbon black is also used to manufacture of various other rubber goods for applications ranging from aerospace to common household goods. Carbon black is available in three grades - soft, hard and super hard.

Exhibit 1: User industries of Carbon Black



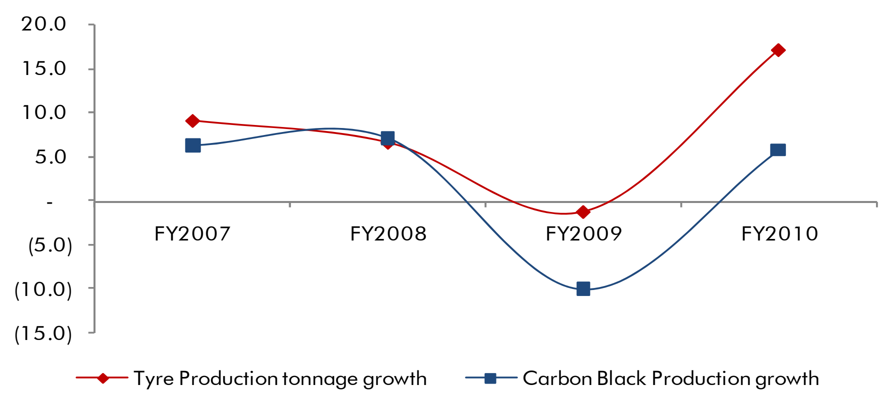
Source: Company, Angel Research

Booming tyre industry to augment demand for carbon black

The tyre industry consumes ~65% of the total carbon black production in India

The fortunes of the carbon black industry are positively correlated with the fortunes of the automotive tyre industry. The tyre industry consumes ~65% of the total carbon black production in India. Carbon black constitutes ~12% of the total raw material expenditure of the tyre companies and forms ~25% of the weight of the tyre.

Exhibit 2: Correlation of tyre and carbon black production



Source: Company, Angel Research

The domestic tyre industry is pegged to be at Rs290bn in FY2010 having posted a CAGR of 16% over FY2005-10. In FY2010, the growth of 25% in value terms was mainly aided by the 19-20% yoy increase in volumes. Going ahead, the automotive tyre sector in India is poised for sharp growth on back of the changing dynamics such as:

- The Government of India's increasing emphasis on improving and expanding the nation's road network, which will translate into higher demand for commercial vehicles going ahead.
- Boom in the two-wheeler and passenger car segments is also being witnessed because of rising consumerism, higher income levels and changing spending patterns in India.
- Incremental demand for tyres is expected to be witnessed in future with India emerging as an automobile manufacturing hub for global majors like Hyundai, Nissan and Toyota.

To bank on this growing opportunity, several tyre players have already announced expansion plans. Over the next three years, the tyre industry is expected to witness investments to the tune of Rs120bn. Crisil Research estimates the tyre industry at Rs600bn by FY2015. In tonnage terms, the demand for tyres is expected to register CAGR of 11-12% over FY2011-15E, which is marginally higher as compared to 10-11% CAGR over FY2005-10. During FY2011E, the tyre off-take in tonnage terms is likely to grow by 13-14%, which is in line with the automobile industry growth estimates. In FY2010, out of the total tyre production in tonnage terms, OEM off-take constituted 24%, while the replacement segment constituted 65% share.

Investment Arguments

Carbon black demand-supply scenario to be favourable

Demand for carbon black to increase at 11.8% CAGR over FY2010-12E

- **Domestic demand to post 9.6% CAGR**

We expect the demand for carbon black from the tyre segment to record 11.3% CAGR over FY2010-12E

The domestic demand for carbon black (excluding imports) is expected to increase at a CAGR of 9.6% over FY2010-12E driven primarily by higher off-take of tyres in tonnage terms. This coupled with the recent imposition of the anti-dumping duty on imported carbon black used in rubber related industries may result in import substitution by the domestic market thereby benefitting domestic players. On the back of the afore-mentioned factors, we expect the demand for carbon black from the tyre segment to record 11.3% CAGR over FY2010-12E.

Non-tyre segment is expected to register CAGR of 6-7% over FY2010-12E

The demand from the non-tyre segment comprising automotive products, moulded and extruded goods and non-rubber user industries like paints, plastics, inks, etc. is linked to the growth of the industrial sector. The non-tyre segment consumes ~35% of the total carbon black production in India and is expected to register CAGR of 6-7% over FY2010-12E.

- **Exports to log CAGR of 25% following shift in production base and rising capacities**

Aditya Birla Nuvo's group company, Hi-tech and PCBL rank 4th and 8th respectively, in the list of largest carbon black producers in the world.

With the global automobile industry moving eastwards to Asia and Eastern Europe, the tyre industry as well as the demand for carbon black have followed suit. This coupled with stringent environmental laws are forcing the closure of some older carbon black capacity in developed regions. As per industry estimates, North America and Western Europe, which produced 48% of the world's carbon black in 1998, are estimated to account for just 23% of the global output in 2013, while the Asia-Pacific region, which produced 36% of the world's carbon black in 1998, will account for ~57% share by 2013. The above-mentioned factors have resulted in many players expanding their capacities in the Asia-Pacific region in turn increasing the export potential from the region. Aditya Birla Nuvo's group company, Hi-tech and PCBL rank 4th and 8th respectively, in the list of largest carbon black producers in the world.

Exhibit 3: Top global producers of carbon black

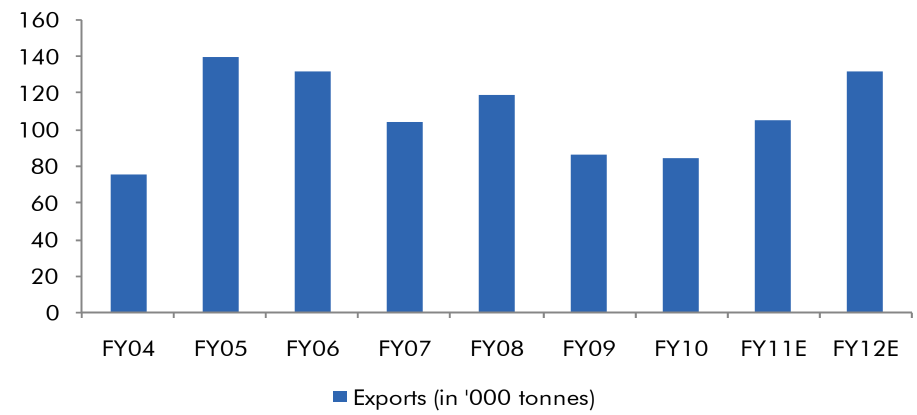
Ranking	Carbon black producers	Capacity (mn tonnes)
1	Cabot USA	2.01
2	Evonik, Germany	1.45
3	Columbia, USA	1.13
4	Aditya Birla Nuvo, India	0.79
5	CSRC, Taiwan	0.74
6	Sid Richardson, USA	0.45
7	Tokai, Japan	0.37
8	PCBL, India	0.35
9	Omsk, Russia	0.35
10	Black Cat, China	0.29

Source: Company, Angel Research

Increase in production will translate in exports increasing at a CAGR of 25% over FY2010-12E

PCBL and Hi-tech , the largest domestic manufacturers of carbon black in India, have chalked out further expansion plans to tap the increasing opportunity going ahead. However, as the demand for the carbon black from the domestic market will catch-up over a period of time, we estimate that the increase in production will translate in exports increasing at a CAGR of 25% over FY2010-12E.

Exhibit 4: Exports set to rise over FY2010-12E



Source: Company, Angel Research

Supply to record CAGR of 8.6% during FY2010-12E, capacity utilisation set to rise

We expect the installed capacity of carbon black to grow at a CAGR of 8.6% on the back of the recently added capacities and ongoing expansion plans. In FY2010, between themselves PCBL and Hi-tech held around ~78% of the total installed capacity in India.

Exhibit 5: Player-wise installed capacity in India

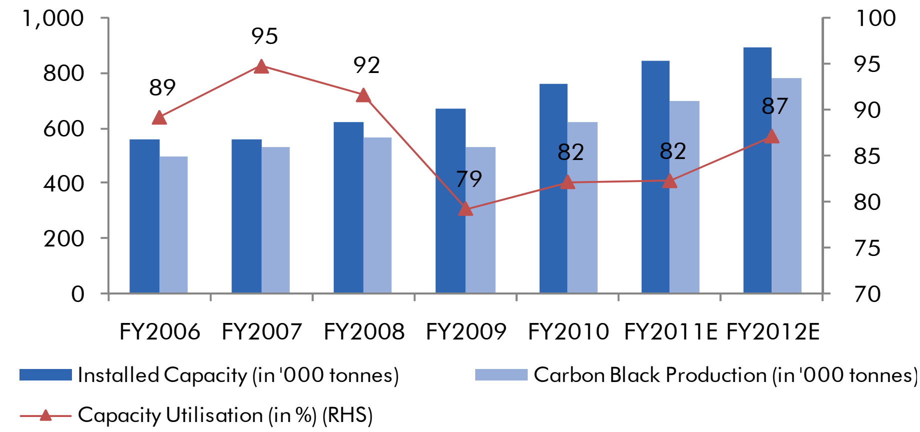
Capacity (tonnes)	FY2010	% share	FY2012E	% share
Phillips Carbon Black	360,000	47.6	410,000	46.5
Hi-Tech	230,000	30.4	315,000	35.8
Cabot*	50,000	6.6	-	-
Continental	66,000	8.7	66,000	7.5
Himadri Chemicals	50,000	6.6	90,000	10.2
Total	**756,000**	**100**	**881,000**	**100**

*Source: Company, Angel Research; *Note: Cabot capacity has been closed and hence not taken into consideration.*

Overall capacity utilisation is likely to rise to ~87% in FY2012E from ~82% in FY2010

On the production front, considering the growth rate in domestic demand (9.6% CAGR over FY2010-12E) and exports (25% CAGR over FY2010-12E), we estimate the carbon black production (after factoring imports) to record CAGR of 11.8% over FY2010-12E. With the rising production trend, the overall capacity utilisation is also likely to rise to ~87% in FY2012E from ~82% in FY2010.

Exhibit 6: Industry capacity, production and utilisation levels



Source: Company, Angel Research

Volume growth backed by capacity expansions to drive top-line

PCBL is setting up a brown-field plant of 50,000MT in Mundra thereby enhancing the installed capacity to 410,000MT

To capitalise on the rising demand for tyres going ahead and consequently carbon black, PCBL has been on an expansion spree. Post commissioning of the 90,000MT green-field plant at Mundra in October 2009, the company's installed capacity jumped from 270,000MT in FY2009 to 360,000MT in FY2010. PCBL has further plans to increase capacity by setting up a brown-field plant of 50,000MT in Mundra thereby enhancing the installed capacity to 410,000MT. The plant is expected to be operational by 3QFY2011E.

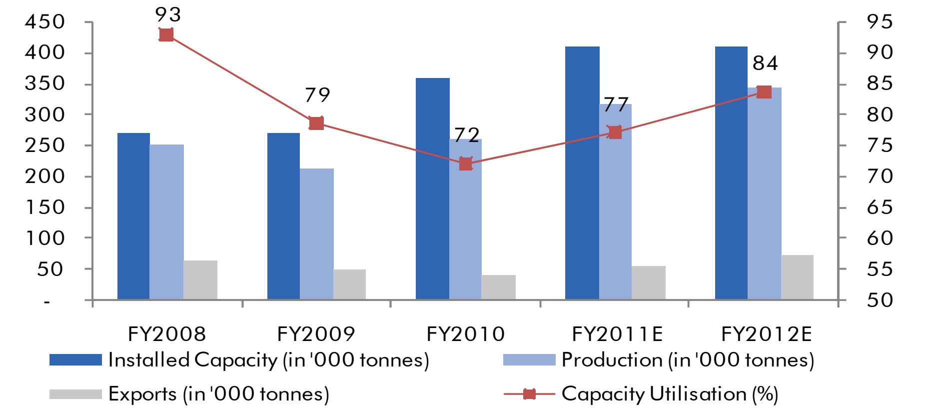
Exhibit 7: Existing capacity and expansion plans

Location	Capacity in MT	Expansion (in MT)	Expanded Capacity	Operational
Durgapur	140,000		140,000	
Baroda	90,000		90,000	
Kochi	40,000		40,000	
Mundra	90,000	50,000	140,000	December 2010
Total Capacity	**360,000**	**50,000**	**410,000**	

Source: Company, Angel Research

With additional capacities coming on stream, we expect the company's volumes to rise by 22.3% and 8.6% in FY2011E and FY2012E respectively, registering a CAGR of 15.3% over FY2010-12E. Factors like rising demand for carbon black from the tyre industry and increasing export potential would be the key drivers for volume growth.

Exhibit 8: Rising capacity, production and exports



Source: Company, Angel Research

During FY2010, PCBL exported 41000MT of carbon black constituting 16% of its total production. The company's exports have picked up post commissioning of the 90,000MT capacity at Mundra. Going ahead, with additional capacity coming up, we expect PCBL's exports, in volume terms, to result in a CAGR of 33.4% over FY2010-12E, thereby constituting 21.3% of the total production.

Accordingly, we expect PCBL's revenues from the carbon black segment to witness CAGR of 22.3% over FY2010-12E

Overseas foray in Vietnam on cards to further tap international markets

Demand for carbon black in Vietnam currently stands at 70,000MT and is expected to be 100,000MT by FY2011E

Following entry of global tyre majors like Kumho and Yokhama and capacity expansions by the Vietnamese tyre companies, globally Vietnam has evolved as a manufacturing hub for tyres. The move is logical for the tyre companies taking into consideration that Vietnam is the fourth largest producer and exporter of rubber. Moreover, Vietnam does not even have a single carbon black manufacturing plant. Thus, to encash on this opportunity PCBL has entered into a 80:20 joint venture with Vietnam National Chemical Corporation for setting up a carbon black facility of 1,00,000MT and a co-generation power plant of 16MW in phases. Demand for carbon black in Vietnam currently stands at 70,000MT and is expected to be 100,000MT by FY2011E. The total capex requirement for the project is estimated to be ~US $65mn and the same will be funded by PCBL and its JV partner in proportion to their respective stakes. PCBL plans to fund its share in the capex through debt-equity of 1:2. However, as the company is at nascent stages of setting up the project and is awaiting certain regulatory approvals and licenses, we have not factored in the same in our financial projections.

Power segment- The game changer

PCBL utilises the off-gas for manufacturing power and hence has no raw material requirement

The carbon black manufacturing process is generally polluting in nature, since the process gas or 'off gas', which is a by-product of the manufacturing process is either released or flared. This requires making additional investments in pollution control equipment to ensure continuous operations. The other option is to convert the gas into steam and use the steam to generate power which can result in three benefits –

- Savings in expenditure associated with flaring the gas,
- Savings in power cost by captively using the electricity generated through the gas, and
- Surplus power generated can be sold to third parties

PCBL set up a 12MW captive power plant (CPP) at Baroda in October 2004 to generate power using the off-gas. After meeting the internal demand for production of carbon black, the surplus power of around 7MW was sold to the Gujarat Electricity Board Grid from end of March 2005. This segment has considerably helped in reducing the company's power cost along with contributing to its revenues.

Encouraged by the success of the Baroda co-generation power plant, the company set up another 30MW co-generation power plant at Durgapur. The company later added another 16MW plant at Mundra along with the carbon black capacity of 90,000MT, which became operational in December 2009. Currently, the company has in place 60.5MW installed capacity. The company further plans to enhance this capacity to 78MW by adding a 10MW plant at Mundra and another 7.5MW plant in Kochi, which are likely to be operational in 3QFY2012E and 2QFY2012E, respectively.

Exhibit 9: Power capacity and expansion plans

Location	Capacity (MW)	Expansion	Operational	Expanded capacity
	FY2010			FY2012E
Baroda	12			12
Durgapur	30			30
Kochi	2.5	7.5	2QFY2012E	10
Mundra	16	10	3QFY2012E	26
Total Capacity	**60.5**	**17.5**		**78**

Source: Company, Angel Research

PCBL would be able to sell ~25.8cr and ~34.3cr units in FY2011 and FY2012, respectively

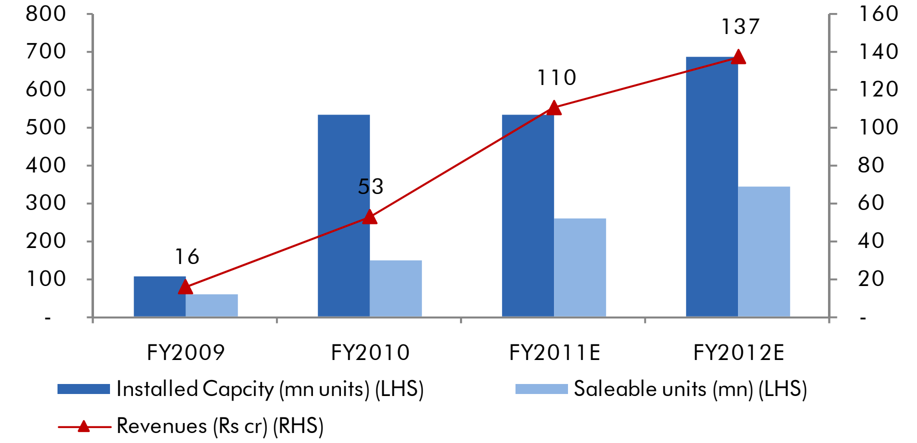
With additional capacities coming on stream, after adjusting for internal consumption requirements, we believe the company would be able to sell ~25.8cr and ~34.3cr units in FY2011 and FY2012, respectively. The company sells the power in open exchanges at spot rates and is likely to get realization of Rs4.3/unit and Rs4/unit in FY2011E and FY2012E respectively. Consequently, we expect PCBL to garner revenues to the tune of Rs110cr and Rs137cr from the power segment in FY2011 and FY2012 respectively, logging a CAGR of 61.6% over FY2010-12E.

Exhibit 10: Power Segment - Revenue and PAT projections

Details	FY2011E	FY2012E
Installed Capacity (in MW)	60.5	78
Installed Capacity (in cr units)	53	68
Production (in cr units)	36	45
Units for captive consumption (in cr) @ 310 units/tonne	10	11
Units sold in open mkt (in cr)	26	34
Realisation / unit (Rs)	4.3	4.0
Revenues (in cr)	**110.2**	**137.2**
Manufacturing Cost per unit (Rs)	0.4	0.4
Manufacturing Cost (Rs cr)	10.3	13.7
EBITDA (in cr)	**99.9**	**123.5**
EBITDA Margin (%)	**90.7**	**90.0**
Int & Dep cost per unit (Rs)	0.4	0.4
Int & Dep cost (Rs cr)	10.3	13.7
PBT (Rs cr)	89.6	109.7
Tax @ 19.9%	17.9	21.9
PAT	**71.7**	**87.9**
PAT Margin (%)	**65.1**	**64.1**

Source: Company, Angel Research

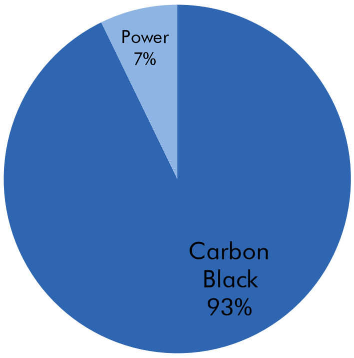
Exhibit 11: Power segment - Revenues picking up



Source: Company, Angel Research

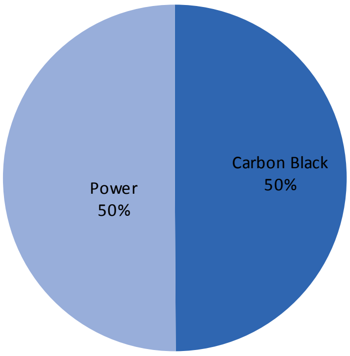
Since PCBL utilises the off-gas for the manufacturing of power, the company has no raw material requirement. This enables the company to earn PBIT margins of 85% on this segment. Thus a high proportion of the power revenues percolate to PBT levels where the company attracts Minimum Alternative Tax (MAT) thereby further boosting up the bottom-line contribution. We estimate the power segment to give phenomenal boost to the company's operating and net profit margins in FY2011E and FY2012E.

Exhibit 12: Revenue contribution - FY2012E



Source: Company, Angel Research

Exhibit 13: Profit contribution - FY2012E



Source: Company, Angel Research

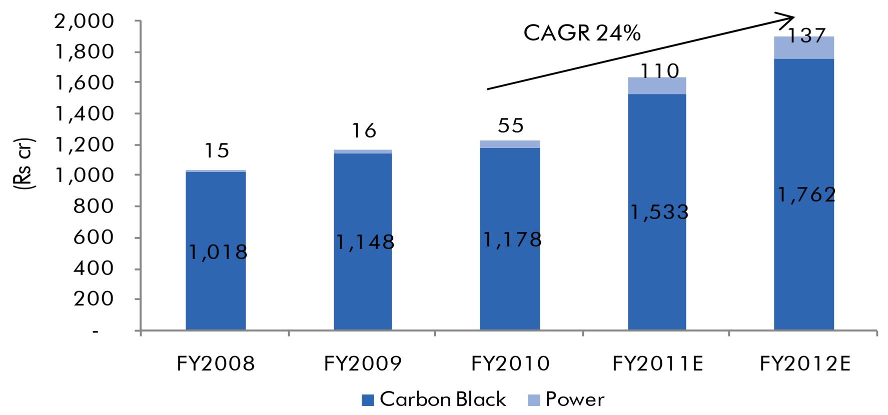
Financial Outlook

Higher carbon black volumes to drive top-line CAGR of 24% over FY2010-12E

Carbon black segment volumes to post a CAGR of 15.3% over FY2010-12E

We expect PCBL's carbon black segment volumes to post a CAGR of 15.3% over FY2010-12E on the back of the recently added Mundra capacity coupled with the other additional capacities also coming up. On the realisation front, we expect PCBL's gross realisation/MT to be in the range of Rs54,000- 57,500 (assuming CBFS prices at US $405/MT and US $438/MT for FY2011E and FY2012E, respectively). PCBL has a price mechanism in place with its customers wherein it either passes on or rolls back the increase/decrease in the raw material (CBFS) costs. Considering the aforesaid factors coupled with increase in capacity utilisation and power segment revenues, we estimate PCBL's revenues to register CAGR of 24% over FY2010-12E.

Exhibit 14: Revenue growth



Source: Company, Angel Research

OPM to improve on higher contribution from power segment

We expect PCBL's EBIDTA to increase from Rs190.4cr in FY2010 to Rs308cr in FY2012 increasing at a CAGR of 27.2% over FY2010-12E. While we expect OPMs of the carbon black segment to be in the range of 10.5-11% over the next two years, we estimate the company's overall margins to come in at 16.1% in FY2011E and 16.2% in FY2012E primarily on the back of the increased contribution from the high-margin power segment percolating to the EBITDA level.

Exhibit 15: Segmental Break-up

Particulars (Rs cr)	FY2008	FY2009	FY2010	FY2011E	FY2012E	CAGR %
Segmental Revenues						
Carbon Black (Net)	1,018	1,148	1,178	1,533	1,762	22.3
% growth	*3.1*	*12.7*	*2.6*	*30.1*	*14.9*	
Power	15	16	55	110	137	58.6
% growth	*41.5*	*3.9*	*252*	*102*	*24.5*	
Total Revenues	1,033	1,163	1,233	1,643	1,899	24.1
Segment Results (PBIT)						
Carbon Black	143.5	(53.3)	142.1	132.9	158.7	5.7
PBIT Margin (%)	*14.1*	*(4.6)*	*12.1*	*8.7*	*9.0*	
% growth	*52.3*	*-*	*-*	*(6.5)*	*19.4*	
Power	11.5	12.3	51.5	93.7	116.6	50.5
PBIT Margin (%)	*77.1*	*79.5*	*94.4*	*85.0*	*85.0*	
% growth	*58.1*	*7.1*	*317.5*	*82.0*	*24.5*	
Total PBIT	155.0	(41.0)	193.6	226.6	275.3	19.2

Source: Company, Angel Research

Exhibit 16: Carbon Black Segment- Key Assumptions

Details	FY2008	FY2009	FY2010	FY2011E	FY2012E
Capacity (in '000 tonnes)	270	270	360	410	410
Production (in '000 tonnes)	250	212	260	316	343
Exports (in '000 tonnes)	65	51	41	55	73
Capacity Utilisation (%)	93	79	72	77	84
Realisation/tonne (Rs)	46,090	60,416	50,395	54,199	57,344

Source: Company, Angel Research

Exhibit 17: Power Segment- Key Assumptions

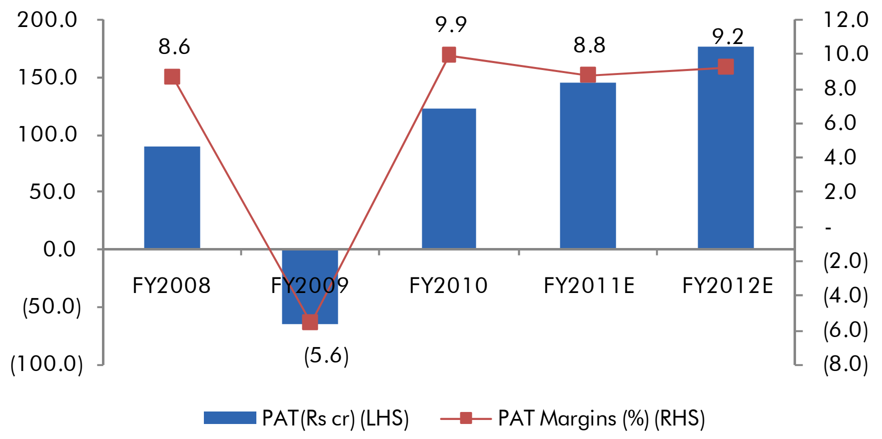
Details	FY2009	FY2010	FY2011E	FY2012E
Installed Capacity (cr units)	10.5	53	53	68
Saleable units (cr units)	5.9	14.6	25.8	34.3
Realisation/unit (Rs)	2.6	3.6	4.3	4.0

Source: Company, Angel Research

PAT to register CAGR of 19.6% over FY2010-12E

We expect PCBL's PAT to grow from Rs122.7cr in FY2010 to Rs175.4cr in FY2012 thereby posting CAGR of 19.6% over the period. However, PAT CAGR is expected to be lower than the EBIDTA CAGR of 27.2% mainly due to rising depreciation costs resulting from new capacities getting operational. Interest cost is however, expected to decline in FY2012E after spiking in FY2011E due to generation of free cash-flows that would be utilised for part repayment of debt. We expect PCBL to record PAT margins of 8.8% and 9.2% in FY2011E and FY2012E, respectively.

Exhibit 18: Net Profit and Net Profit Margins



Source: Company, Angel Research

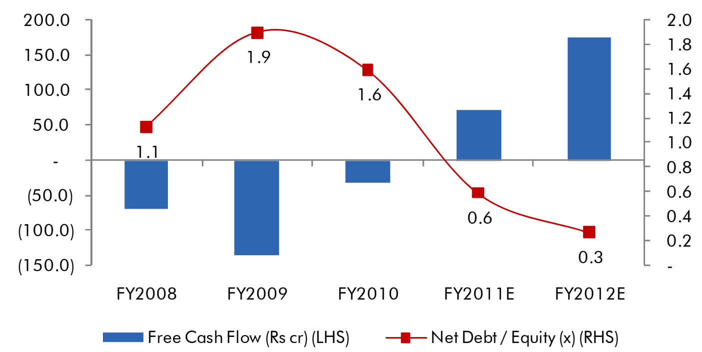
Capex funding in place

PCBL is in the process of setting up additional 50,000MT capacity carbon black plant in Mundra along with two power plants of 10MW and 7.5MW capacity each at Mundra and Kochi, respectively. Funds required for such expansion would be to the tune of Rs155cr. The company through a QIP issue has already raised Rs100cr at Rs200/share. The promoters have also subscribed to 12.5mn warrants at Rs196 each further raising ~Rs25cr. Thus, Rs125cr is already in place and the company proposes to meet the balance requirements through internal accruals. Post the fund raising, the company's equity capital would stand diluted at Rs34.5cr.

Debt/equity ratio to taper down, return ratios to improve

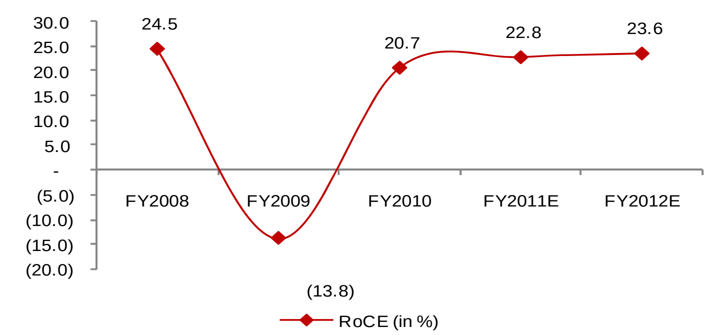
We estimate PCBL to generate robust free cash-flows of Rs73cr and Rs170cr in FY2011E and FY2012E, respectively. Consequently, the company's debt burden is expected to reduce from ~Rs550cr in FY2010 to Rs400cr in FY2012 thereby lowering the Net debt-equity ratio to ~0.3x from ~1.6x in FY2010. With higher contribution from the high-margin power segment percolating to the bottom-line coupled with tapering debt over FY2010-12E, we estimate PCBL to witness an improvement in the return ratios. Accordingly, we expect PCBL's RoCE to rise from 20.7% in FY2010 to 23.6% in FY2012.

Exhibit 19: Free Cash Flow & Debt-Equity Ratio



Source: Company, Angel Research

Exhibit 20: Improving RoCE's



Source: Company, Angel Research

Concerns

Slowdown in tyre industry

The fortunes of the carbon black industry are to a large extent positively co-related with the fortunes of the tyre industry. Hence, any slowdown in the tyre industry may lead to lower demand and in turn impact the company's performance.

Abrupt downward movement in crude prices

Carbon Black Feedstock (CBFS), a crude derivative, is the major raw material required in the manufacture of carbon black constituting ~80-85% of the total raw material costs. Prices of CBFS are positively co-related with the crude prices, as 60-65% of the CBFS cost is the price of crude. Therefore, extreme fluctuations in the crude prices affect the margins of carbon black producers.

Even though PCBL has price mechanism in place with its customers, any abrupt downward movement in the crude prices, like one witnessed in FY2009, hampers the company's performance as it may not be able to roll back its prices substantially thereby providing its customers an arbitrage opportunity to import carbon black.

Exchange rate fluctuations

The company majorly imports its raw material requirement. While the company has a hedging policy, any abrupt movement in currency rates could hit margins.

Delays in execution of upcoming capacities

PCBL is in expansion mode and any delays in timely execution of the upcoming capacities may affect the company's financial performance and our estimates.

Outlook and Valuation

Fortunes of the carbon black industry are positively co-related with the fortunes of the automotive tyre industry. In tonnage terms, the demand for tyres is expected to record a CAGR of 11-12% over FY2011-12E, which is marginally higher than the 10-11% CAGR registered over FY2005-10. Going ahead, India is expected to emerge as an automobile manufacturing hub for global majors like Hyundai, Nissan and Toyota on the back of which we expect tyres to register incremental demand. Overall, we estimate the domestic carbon black industry to clock demand at a CAGR of 9.6% over FY2010-12E. Moreover, shifting of capacities from the western world to the Asia-Pacific region would result in increased potential for exports.

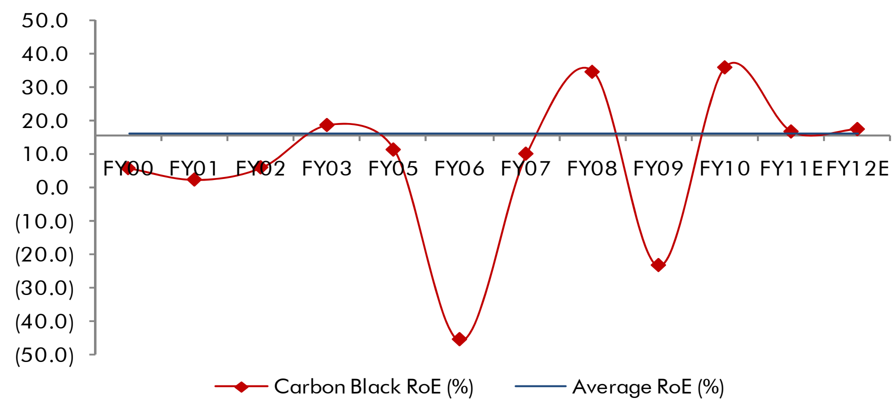
Considering PCBL's capacity addition plans and its dominant position in the carbon black industry, we believe it is well poised to capitalise on the increasing demand for carbon black going ahead. Moreover, the company's power segment is expected to contribute significantly to its profitability and lend stability to the company's earnings coupled with significantly de-risking its business model. Thus, we are bullish on the company's growth prospects over FY2010-12E

We have valued PCBL on the sum-of-the-parts (SOTP) methodology wherein we have valued its carbon black and power segments independently.

Carbon black segment valuation

Gauging its historical performance, PCBL's carbon black segment has been able to generate RoE's at an average of ~16% (post adjusting for abnormal periods), thereby justifying the P/BV multiple above 1x. With demand of carbon black estimated to witness a CAGR of 11.8% over FY2010-12E, we expect the company to maintain the RoE's of 16% going ahead. However, considering the commodity nature of the business, we have conservatively valued PCBL's carbon black segment at 1x FY2012E P/BV. We thereby arrive at the value of Rs144/share for PCBL's carbon black segment.

Exhibit 21: Carbon Black Segment RoE's



Source: Company, Angel Research

Power segment valuation

We have valued PCBL's power segment using the NPV methodology, considering its stable revenues. We have thereby derived a value of Rs126/share for the power segment.

Exhibit 22: NPV of Power Segment

(Rs cr)	FY11E	FY12E	FY13E	FY14E	FY15E	FY16E	FY17E	FY18E	FY19E	FY20E
Units sold in open mkt (in cr)	25.8	34.3	34.3	34.3	34.3	34.3	34.3	34.3	34.3	34.3
Realisation / unit (Rs)	4.3	4.0	3	3.1	3.1	3.2	3.3	3.3	3.4	3.5
Revenues	110.2	137.2	102.9	105.5	107.6	109.7	111.9	114.2	116.4	118.8
Cost per unit incl int & Dep	0.8	0.8	0.8	0.9	0.9	1.0	1.0	1.1	1.1	1.2
PBT	89.6	109.7	74.1	75.2	75.8	76.4	76.9	77.4	77.8	78.2
Tax @19.9%	17.9	21.9	14.8	15.0	15.1	15.2	15.3	15.4	15.5	15.6
PAT	71.8	87.9	59.3	60.2	60.7	61.1	61.6	62.0	62.3	62.6
Total	71.8	87.9	59.3	60.2	60.7	61.1	61.6	62.0	62.3	62.6
Discounting Factor	0.9	0.7	0.6	0.6	0.5	0.4	0.4	0.3	0.3	0.2
NPV	62.0	65.6	38.2	33.5	29.2	25.4	22.1	19.2	16.7	14.5

Source: Company, Angel Research; Note: Power Segment has a negative working capital requirement. We have not considered the same to be conservative. Including the working capital effect can provide further upside to the valuations.

Exhibit 23: Cost of Equity & Terminal Growth Rate Assumptions

Details	
Risk Free rate (%)	7.5
Market Return (%)	14.5
Beta	1.2
Cost of Equity (%)	15.8
Terminal Growth (%)	2.0

Source: Company, Angel Research

Exhibit 24: Fair Value of Power Segment

Details	(Rs cr)
NPV of PAT (FY2011E-FY2020E)	327
(+) terminal cash flows	108
Fair Value of Power Segment	434
Number of shares	3.5
Fair Value/share	126

Source: Company, Angel Research

Exhibit 25: PCBL's SOTP Valuation

Segment	Value/Share (Rs)
Carbon Black Segment	144
Power Business	126
Total Value per share	270

Source: Company, Angel Research

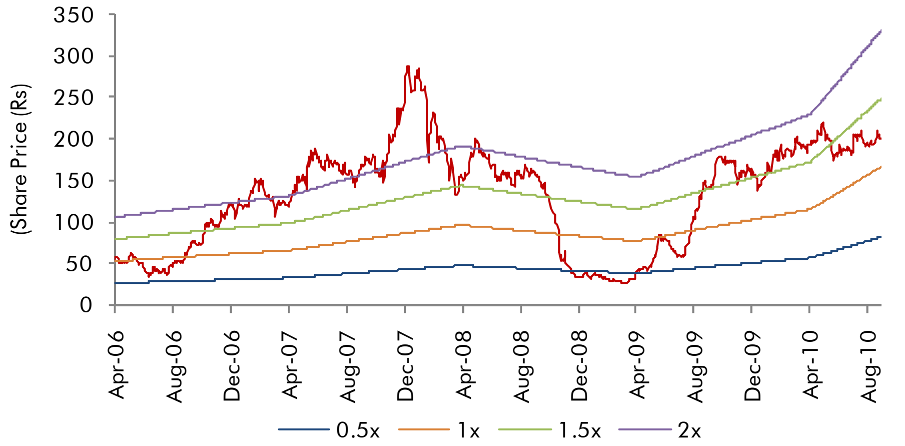
At the CMP, the stock is trading at promising valuations of 4.2x FY2012E EPS of Rs50.9 and 1x FY2012E P/BV on diluted capital. Additionally, with the power segment expected to contribute significantly to profitability we believe the stock to be ideally poised for re-rating. **We re-initiate coverage on the stock with a Buy recommendation and SOTP-based Target Price of Rs270.**

Exhibit 26: Peer Comparison

Company	Mcap	P/BV (x)		PE (x)		EV/EBITDA (x)		RoE (%)	
	(USD mn)	FY2011E	FY2012E	FY2011E	FY2012E	FY2011E	FY2012E	FY2011E	FY2012E
Black Cat, China	479	3.1	2.6	14.6	15.1	12.4	10.7	22.3	21.4
Tokai Carbon, Japan	1,381	1.0	0.9	14.4	11.6	4.9	5.1	8.4	8.0
PCBL, India	151	1.3	1.0	5.1	4.2	4.0	3.0	31.7	26.6

*Source: Company, Angel Research. Note- * Bloomberg Estimates*

Exhibit 27: One-year forward P/BV band



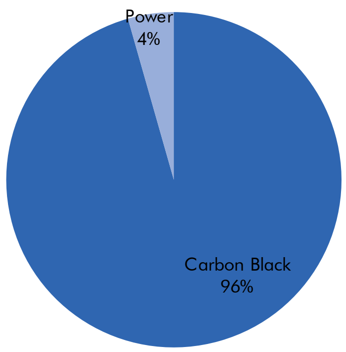
Source: Company, Angel Research

Company Background

PCBL, part of the RPG group, is the leading producer of carbon black in the country. The company is not only the largest exporter of carbon black from India, but is also one of the largest players in this field in Asia. The company started production in 1962 using the oil furnace, which was then the most widely accepted manufacturing process of carbon black, patented by its collaborator and world carbon black leader, Phillips Petroleum Company, USA. In 1988, PCBL entered into a technical agreement with Columbian Chemicals Company, USA, and acquired access to the state-of-the-art carbon black technology, helping the company gain flexibility, product range, production capacity and energy conservation.

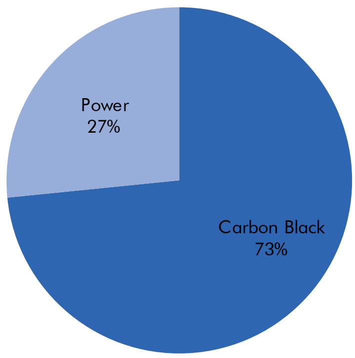
The company has an installed capacity of 3,60,000MT, which constitutes ~48% of the total installed capacity in India. PCBL has four manufacturing units located in Durgapur (1,40,000MT), Cochin (40,000MT), Baroda (90,000MT) and Mundra (90000MT). The company further plans to add 50000MT capacity plat in Mundra. With a view to generate power from the off-gas generated while manufacturing carbon black, PCBL set up a 12MW co-generation power plant in Baroda in October 2004. Encouraged by the success of the Baroda co-generation power plant, the company set up additional co-generation power plants at its Durgapur and Mundra facility, thereby enhancing the capacity to 60.5MW in FY2010E. The company further plans to add 17.5MW capacity in Mundra (10MW) and Kochi (7.5MW) thereby enhancing the power generating capacity to 78MW going ahead.

Exhibit 28: Sales Break-up (FY2010)



Source: Company, Angel Research

Exhibit 29: PBIT Break-up (FY2010)



Source: Company, Angel Research

Profit & Loss Statement

Y/E March (Rs cr)	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
Net Sales	999	1,033	1,163	1,235	1,643	1,899
Total operating income	999	1,033	1,163	1,235	1,643	1,899
% chg	*37.1*	*3.5*	*12.6*	*6.0*	*33.3*	*15.6*
Total Expenditure	903	887	1,228	1,045	1,378	1,591
Net Raw Materials	679	634	930	869	1,100	1,260
Other Mfg costs	40	41	38	36	53	65
Personnel	24	29	35	37	44	51
Other	160	183	225	103	181	216
EBITDA	**96**	**146**	**(65)**	**190**	**265**	**308**
% chg	*213.0*	*52.3*	-	-	*39.3*	*16.1*
(% of Net Sales)	*9.6*	*14.2*	-	*15.4*	*16.1*	*16.2*
Depreciation& Amortisation	20	20	20	31	39	43
EBIT	**76**	**126**	**(84)**	**159**	**227**	**265**
% chg	*642.3*	*66.7*	*(166.7)*	-	*42.3*	*16.9*
(% of Net Sales)	*7.6*	*12.2*	*(7.2)*	*12.9*	*13.8*	*13.9*
Interest & other Charges	37	19	29	29	35	28
Other Income	6	6	16	0	6	4
(% of PBT)	13.8	5.4	(18.1)	0.2	3.0	1.7
Recurring PBT	**44**	**113**	**(90)**	**131**	**197**	**240**
% chg	-	*154.1*	-	*245.2*	*51.0*	*21.9*
Extraordinary Income/(Exp.)	(0)	(0)	7	-	-	-
PBT (reported)	**45**	**113**	**(97)**	**131**	**197**	**240**
Tax	21	23	(32)	8	53	65
(% of PBT)	*47.2*	*20.8*	-	*6.0*	*27.1*	*27.0*
PAT (reported)	**24**	**89**	**(65)**	**123**	**144**	**175**
ADJ. PAT	**24**	**90**	**(72)**	**123**	**144**	**175**
% chg	-	*276.6*	-	-	*17.2*	*22.0*
(% of Net Sales)	*2.4*	*8.7*	-	*9.9*	*8.8*	*9.2*
Basic EPS (Rs)	**9.4**	**35.5**	**(25.5)**	**43.4**	**41.7**	**50.9**
Fully Diluted EPS (Rs)	**9.4**	**35.5**	**(25.5)**	**43.4**	**41.7**	**50.9**
% chg	-	*276.6*	-	-	*(3.9)*	*22.0*

Balance Sheet

Y/E March (Rs cr)	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
SOURCES OF FUNDS						
Equity Share Capital	25	25	28	28	34	34
Preference Capital	-	1	2	3	4	5
Reserves& Surplus	141	218	190	296	541	699
Shareholders Funds	**166**	**244**	**220**	**327**	**579**	**739**
Total Loans	250	290	426	555	505	405
Deferred Tax Liability	43	35	2	10	10	10
Total Liabilities	**459**	**570**	**647**	**892**	**1,094**	**1,154**
APPLICATION OF FUNDS						
Gross Block	447	451	440	828	920	980
Less: Acc. Depreciation	187	206	213	235	273	317
Net Block	**260**	**245**	**228**	**593**	**647**	**664**
Capital Work-in-Progress	21	131	383	92	60	40
Goodwill	-	1	2	3	4	5
Investments	**28**	**28**	**38**	**38**	**38**	**38**
Current Assets	467	450	393	674	976	1,135
Cash	42	15	7	33	163	196
Loans & Advances	76	62	84	149	156	180
Other	349	373	302	492	657	760
Current liabilities	318	286	397	508	630	728
Net Current Assets	**149**	**164**	**(4)**	**166**	**346**	**407**
Mis. Exp. not written off	1	1	1	-	-	-
Total Assets	**459**	**570**	**647**	**892**	**1,094**	**1,154**

Cash Flow Statement

Y/E March (Rs cr)	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
Profit before tax	45	113	(97)	131	197	240
Depreciation	20	20	20	31	39	43
Change in Working Capital	(71)	(57)	183	(79)	(43)	(4)
Less: Other income	6	6	16	0	6	4
Direct taxes paid	21	23	(32)	8	53	65
Cash Flow from Operations	**(33)**	**46**	**121**	**75**	**133**	**210**
(Inc)./ Dec in Fixed Assets	(88)	(114)	(255)	(106)	(60)	(40)
(Inc)./ Dec in Investments	(14)	-	(10)	(0)	-	-
(Inc)/ Dec in loans and advances	(37)	14	(23)	(65)	(6)	(24)
Other income	6	6	16	0	6	4
Cash Flow from Investing	**(133)**	**(94)**	**(271)**	**(171)**	**(60)**	**(60)**
Issue of Equity	13	-	3	-	6	-
Inc./(Dec.) in loans	164	40	135	130	(50)	(100)
Dividend Paid (Incl. Tax)	(25)	(51)	-	(71)	(86)	(86)
Others	43	30	4	63	187	69
Cash Flow from Financing	**195**	**20**	**142**	**122**	**57**	**(117)**
Inc./(Dec.) in Cash	28	(27)	(8)	26	130	33
Opening Cash balances	**14**	**42**	**15**	**7**	**33**	**163**
Closing Cash balances	**42**	**15**	**7**	**33**	**163**	**196**

Key Ratios

Y/E March	FY2007	FY2008	FY2009	FY2010	FY2011E	FY2012E
Valuation Ratio (x)						
P/E (on FDEPS)	22.6	6.0	(8.3)	4.9	5.1	4.2
P/CEPS	12.2	4.9	(11.5)	3.9	4.0	3.4
P/BV	3.2	2.2	2.7	1.8	1.3	1.0
Dividend yield (%)	0.9	1.9	-	2.3	2.3	2.3
EV/Sales	0.9	1.0	1.0	1.0	0.6	0.5
EV/EBITDA	9.5	6.7	(17.4)	6.5	4.0	3.0
EV / Total Assets	2.0	1.7	1.7	1.4	1.0	0.8
Per Share Data (Rs)						
EPS (Basic)	9.4	35.5	-	43.4	41.7	50.9
EPS (fully diluted)	9.4	35.5	-	43.4	41.7	50.9
Cash EPS	17.5	43.4	-	54.5	53.0	63.4
DPS	2.0	4.0	-	5.0	5.0	5.0
Book Value	65.7	96.6	77.9	115.9	168.1	214.3
Dupont Analysis						
EBIT margin	7.6	12.2	(7.2)	12.9	13.8	13.9
Tax retention ratio	52.8	79.2	100.0	94.0	72.9	73.0
Asset turnover (x)	2.2	1.8	1.8	1.4	1.5	1.6
ROIC (Post-tax)	8.7	17.5	-	16.8	15.1	16.8
Cost of Debt (Post Tax)	11.7	5.7	8.2	5.5	4.9	4.5
Leverage (x)	0.9	1.2	1.5	1.7	1.0	0.4
Operating ROE	6.1	31.5	-	36.0	24.9	21.9
Returns (%)						
ROCE (Pre-tax)	21.5	24.5	-	20.7	22.8	23.6
Angel ROIC (Pre-tax)	19.1	29.7	-	20.8	26.0	28.9
ROE	15.0	43.7	-	44.8	31.7	26.6
Turnover ratios (x)						
Asset Turnover (Gross Block)	2.8	2.3	2.6	1.9	1.9	2.0
Inventory / Sales (days)	38	48	43	47	59	70
Receivables (days)	84	80	62	70	68	66
Payables (days)	101	113	100	155	145	150
WC cycle (ex-cash) (days)	19	45	22	18	35	38
Solvency ratios (x)						
Net debt to equity	1.3	1.1	1.9	1.6	0.6	0.3
Net debt to EBITDA	2.2	1.9	(6.5)	2.7	1.3	0.7
Interest Coverage (EBIT / Interest)	2.0	6.5	(2.9)	5.5	6.4	9.3

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1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below Rs 1 lakh for Angel, its Group companies and Directors.

Ratings (Returns) :	*Buy (> 15%)*	*Accumulate (5% to 15%)*	*Neutral (-5 to 5%)*
	Reduce (-5% to 15%)	Sell (< -15%)	

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