

EARNINGS REVIEW

Asian Paints (India) (ASPN.BO)

Neutral

Equity Research

Below expectations: EBIT miss on negative operating leverage

What surprised us

Asian Paints (ASPN) reported 1QFY14 PAT of Rs2.9bn (-5% yoy, -19% vs GSe). While sales were broadly in line, the PAT miss was due to higher SG&A. Key takeaways: **1) Volumes:** Based on RM (raw materials) costs inflation, we calculate volume growth of 11-12%, against a lower base in 1QFY13. Management expects double-digit yoy volume growth for FY14 on account of a good monsoon; **2) ASPN took a 1.15% price increase** on May 1, and will take a further 1% price increase on August 1; **3) Gross margin** for the quarter rose by 164bps yoy as RM costs remained benign. However, EBIT margin fell 106bps yoy due to higher SG&A. Depreciation rose due to installation of the Khandala plant. One-offs in employee costs (Rs100mn for re-evaluation of pension liability at a lower discounting rate) and other expenses (Rs140mn for FX impact) had a total negative impact of Rs240mn on PBT; **4) Tax rate** for the quarter was higher yoy at 32.8% due to a surcharge imposition. ASPN expects a similar tax rate for FY14; **5) ASPN expects 30-35% utilization of the Khandala plant** for FY14.

What to do with the stock

We lower our FY14-16E EPS by 3-6% to reflect higher SG&A and tax rate. Hence, we cut our 12m P/E-based (26X, unchanged) TP to Rs4,130 from (Rs4,258). We forecast FY13-16E EPS CAGR of 16% vs 5-yr historical CAGR of 22% (10-yr: 23%). On our estimates, ASPN is trading at 12m fwd P/E of 34.6X, vs 3-yr historical average of 29.3X (10-yr 21.7X), but in line with the sector average FY14E P/E of 36X. Maintain **Neutral**. **Key risks:** Upside: Faster-than-expected volume growth; sharp correction in input cost prices; Downside: competitive pressure; slower growth in international business.

Asian Paints 1QFY14 results summary

| Rs mn | 1QFY14 Actual | 1QFY14 GSe | var | 1QFY13 Actual | yoy | 4QFY13 Actual | qoq |
|--------------|------------------|---------------|------|------------------|-----|------------------|-----|
| Net sales | 28,183 | 27,946 | 1% | 25,393 | 11% | 27,137 | 4% |
| EBIT | 4,288 | 4,787 | -10% | 4,131 | 4% | 3,442 | 25% |
| Adjusted PAT | 2,850 | 3,503 | -19% | 2,989 | -5% | 2,589 | 10% |

Source: Company data, Goldman Sachs Research estimates

INVESTMENT LIST MEMBERSHIP

Neutral

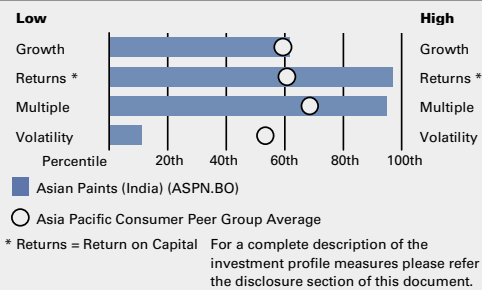
Coverage View: Neutral

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Investment Profile



| Key data | Current |
|------------------------------|---------------------|
| Price (Rs) | 5,076.90 |
| 12 month price target (Rs) | 4,130.00 |
| Market cap (Rs mn / US\$ mn) | 486,975.1 / 8,170.0 |
| Foreign ownership (%) | -- |

| | 3/13 | 3/14E | 3/15E | 3/16E |
|--------------------|--------|--------|--------|--------|
| EPS (Rs) New | 116.13 | 133.68 | 158.85 | 180.47 |
| EPS revision (%) | 0.0 | (5.9) | (3.0) | (4.1) |
| EPS growth (%) | 12.7 | 15.1 | 18.8 | 13.6 |
| EPS (dil) (Rs) New | 116.13 | 133.68 | 158.85 | 180.47 |
| P/E (X) | 34.5 | 38.0 | 32.0 | 28.1 |
| P/B (X) | 11.3 | 12.2 | 10.4 | 9.0 |
| EV/EBITDA (X) | 22.0 | 23.3 | 20.1 | 17.5 |
| Dividend yield (%) | 1.3 | 1.4 | 1.7 | 2.1 |
| ROE (%) | 36.3 | 34.8 | 35.2 | 34.4 |
| CROCI (%) | 37.2 | 37.6 | 40.2 | 40.4 |

Price performance chart



| Share price performance (%) | 3 month | 6 month | 12 month |
|-----------------------------|---------|---------|----------|
| Absolute | 9.3 | 15.4 | 36.3 |
| Rel. to India BSE30 Sensex | 4.0 | 14.4 | 16.0 |

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 7/22/2013 close.

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Asian Paints (India): Summary Financials

| Profit model (Rs mn) | 3/13 | 3/14E | 3/15E | 3/16E | Balance sheet (Rs mn) | 3/13 | 3/14E | 3/15E | 3/16E |
|---|------------------|------------------|------------------|------------------|---------------------------------------|-----------------|-----------------|-----------------|-----------------|
| Total revenue | 109,707.4 | 125,780.2 | 142,888.0 | 162,374.9 | Cash & equivalents | 7,519.8 | 14,170.5 | 18,850.2 | 23,326.3 |
| Cost of goods sold | (65,930.5) | (73,141.2) | (82,946.5) | (94,177.4) | Accounts receivable | 9,808.8 | 9,304.3 | 10,569.8 | 12,011.3 |
| SG&A | (25,964.6) | (31,948.2) | (35,941.8) | (40,803.0) | Inventory | 18,302.9 | 20,304.6 | 23,026.7 | 26,144.5 |
| R&D | -- | -- | -- | -- | Other current assets | 4,433.5 | 4,433.5 | 4,433.5 | 4,433.5 |
| Other operating profit/(expense) | (2,038.9) | (2,515.6) | (2,857.8) | (3,247.5) | Total current assets | 40,065.0 | 48,212.9 | 56,880.1 | 65,915.6 |
| EBITDA | 17,319.4 | 20,439.3 | 23,571.0 | 26,826.2 | Net PP&E | 24,248.9 | 25,758.3 | 27,615.8 | 29,807.9 |
| Depreciation & amortization | (1,546.0) | (2,264.0) | (2,429.1) | (2,679.2) | Net intangibles | 310.6 | 310.6 | 310.6 | 310.6 |
| EBIT | 15,773.4 | 18,175.2 | 21,141.9 | 24,147.0 | Total investments | 1,501.2 | 1,501.2 | 1,501.2 | 1,501.2 |
| Interest income | 137.3 | 137.3 | 137.3 | 137.3 | Other long-term assets | 1,763.9 | 1,763.9 | 1,763.9 | 1,763.9 |
| Interest expense | (366.5) | (285.2) | (285.2) | (285.2) | Total assets | 67,889.6 | 77,546.9 | 88,071.6 | 99,299.2 |
| Income/(loss) from uncons. subs. | 0.0 | 0.0 | 0.0 | 0.0 | Accounts payable | 14,415.7 | 16,527.7 | 18,775.7 | 21,336.3 |
| Others | 1,007.9 | 1,500.0 | 1,750.0 | 1,750.0 | Short-term debt | 1,898.6 | 1,898.6 | 1,898.6 | 1,898.6 |
| Pretax profits | 16,552.1 | 19,527.3 | 22,744.0 | 25,749.1 | Other current liabilities | 12,999.8 | 13,999.8 | 14,999.8 | 15,999.8 |
| Income tax | (4,956.9) | (6,248.7) | (7,050.6) | (7,982.2) | Total current liabilities | 29,314.1 | 32,426.1 | 35,674.1 | 39,234.7 |
| Minorities | (456.4) | (456.4) | (456.4) | (456.4) | Long-term debt | 478.0 | 478.0 | 478.0 | 478.0 |
| Net income pre-preferred dividends | 11,138.8 | 12,822.2 | 15,237.0 | 17,310.5 | Other long-term liabilities | 2,646.9 | 2,646.9 | 2,646.9 | 2,646.9 |
| Preferred dividends | 0.0 | 0.0 | 0.0 | 0.0 | Total long-term liabilities | 3,124.9 | 3,124.9 | 3,124.9 | 3,124.9 |
| Net income (pre-exceptionals) | 11,138.8 | 12,822.2 | 15,237.0 | 17,310.5 | Total liabilities | 32,439.0 | 35,551.0 | 38,799.0 | 42,359.6 |
| Post-tax exceptionals | 0.0 | 0.0 | 0.0 | 0.0 | Preferred shares | 0.0 | 0.0 | 0.0 | 0.0 |
| Net income | 11,138.8 | 12,822.2 | 15,237.0 | 17,310.5 | Total common equity | 33,842.9 | 39,931.8 | 46,752.2 | 53,962.7 |
| EPS (basic, pre-exception) (Rs) | 116.13 | 133.68 | 158.85 | 180.47 | Minority interest | 1,607.7 | 2,064.1 | 2,520.5 | 2,976.9 |
| EPS (basic, post-exception) (Rs) | 116.13 | 133.68 | 158.85 | 180.47 | Total liabilities & equity | 67,889.6 | 77,546.9 | 88,071.6 | 99,299.2 |
| EPS (diluted, post-exception) (Rs) | 116.13 | 133.68 | 158.85 | 180.47 | BVPS (Rs) | 352.83 | 416.30 | 487.41 | 562.58 |
| DPS (Rs) | 53.82 | 70.20 | 87.75 | 105.30 | | | | | |
| Dividend payout ratio (%) | 46.3 | 52.5 | 55.2 | 58.3 | | | | | |
| Free cash flow yield (%) | 1.4 | 2.6 | 2.5 | 2.8 | | | | | |
| Growth & margins (%) | 3/13 | 3/14E | 3/15E | 3/16E | Ratios | 3/13 | 3/14E | 3/15E | 3/16E |
| Sales growth | 13.9 | 14.7 | 13.6 | 13.6 | CROCI (%) | 37.2 | 37.6 | 40.2 | 40.4 |
| EBITDA growth | 14.8 | 18.0 | 15.3 | 13.8 | ROE (%) | 36.3 | 34.8 | 35.2 | 34.4 |
| EBIT growth | 13.7 | 15.2 | 16.3 | 14.2 | ROA (%) | 17.6 | 17.6 | 18.4 | 18.5 |
| Net income growth | 12.7 | 15.1 | 18.8 | 13.6 | ROACE (%) | 41.8 | 44.2 | 50.1 | 52.0 |
| EPS growth | 12.7 | 15.1 | 18.8 | 13.6 | Inventory days | 94.9 | 96.3 | 95.3 | 95.3 |
| Gross margin | 39.9 | 41.9 | 42.0 | 42.0 | Receivables days | 29.3 | 27.7 | 25.4 | 25.4 |
| EBITDA margin | 15.8 | 16.3 | 16.5 | 16.5 | Payable days | 75.8 | 77.2 | 77.7 | 77.7 |
| EBIT margin | 14.4 | 14.5 | 14.8 | 14.9 | Net debt/equity (%) | (14.5) | (28.1) | (33.4) | (36.8) |
| | | | | | Interest cover - EBIT (X) | 68.8 | 122.9 | 143.0 | 163.3 |
| Cash flow statement (Rs mn) | 3/13 | 3/14E | 3/15E | 3/16E | Valuation | 3/13 | 3/14E | 3/15E | 3/16E |
| Net income pre-preferred dividends | 11,138.8 | 12,822.2 | 15,237.0 | 17,310.5 | P/E (analyst) (X) | 34.5 | 38.0 | 32.0 | 28.1 |
| D&A add-back | 1,546.0 | 2,264.0 | 2,429.1 | 2,679.2 | P/B (X) | 11.3 | 12.2 | 10.4 | 9.0 |
| Minorities interests add-back | 0.0 | 0.0 | 0.0 | 0.0 | EV/EBITDA (X) | 22.0 | 23.3 | 20.1 | 17.5 |
| Net (inc)/dec working capital | (1,586.7) | 614.8 | (1,739.6) | (1,998.7) | EV/GCI (X) | 9.3 | 11.0 | 9.8 | 8.7 |
| Other operating cash flow | 822.6 | 670.9 | 614.7 | 614.7 | Dividend yield (%) | 1.3 | 1.4 | 1.7 | 2.1 |
| Cash flow from operations | 11,920.7 | 16,371.8 | 16,541.2 | 18,605.7 | | | | | |
| Capital expenditures | (6,437.8) | (3,773.4) | (4,286.6) | (4,871.2) | | | | | |
| Acquisitions | 0.0 | 0.0 | 0.0 | 0.0 | | | | | |
| Divestitures | 70.6 | 0.0 | 0.0 | 0.0 | | | | | |
| Others | 1,730.2 | 0.0 | 0.0 | 0.0 | | | | | |
| Cash flow from investments | (4,637.0) | (3,773.4) | (4,286.6) | (4,871.2) | | | | | |
| Dividends paid (common & pref) | (4,620.5) | (5,947.7) | (7,574.9) | (9,258.3) | | | | | |
| Inc/(dec) in debt | (1,015.6) | 0.0 | 0.0 | 0.0 | | | | | |
| Common stock issuance (repurchase) | 0.0 | 0.0 | 0.0 | 0.0 | | | | | |
| Other financing cash flows | (370.9) | 0.0 | 0.0 | 0.0 | | | | | |
| Cash flow from financing | (6,007.0) | (5,947.7) | (7,574.9) | (9,258.3) | | | | | |
| Total cash flow | 1,276.7 | 6,650.7 | 4,679.7 | 4,476.2 | | | | | |

Note: Last actual year may include reported and estimated data.
Source: Company data, Goldman Sachs Research estimates.

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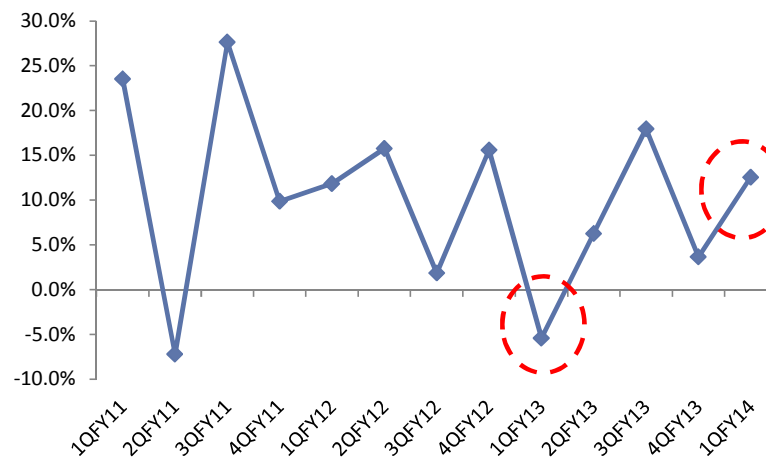
Exhibit 1: While sales were broadly in line, the PAT miss was due to higher SG&A
Summary of 1QFY14 results

| | Actual | GSe | | Actual | | Actual | |
|--------------------------------|---------------|---------------|-------------|---------------|------------|---------------|------------|
| Net sales | 28,183 | 27,946 | 1% | 25,393 | 11% | 27,137 | 4% |
| Other Operating Income | 228 | - | | 87 | | 195 | |
| COGS | 16,138 | 15,510 | | 14,838 | | 15,523 | |
| Gross Profit | 12,273 | 12,436 | -1% | 10,641 | 15% | 11,808 | 4% |
| Staff Cost | 1,909 | 1,850 | 3% | 1,586 | 20% | 1,601 | 19% |
| Other expenditure | 5,478 | 5,310 | 3% | 4,590 | 19% | 6,277 | -13% |
| EBITDA | 4,887 | 5,276 | -7% | 4,466 | 9% | 3,930 | 24% |
| Depreciation | 599 | 489 | | 334 | 79% | 489 | 23% |
| EBIT | 4,288 | 4,787 | -10% | 4,131 | 4% | 3,442 | 25% |
| Exceptionals | (240) | - | | - | | - | |
| Other income | 277 | 284 | | 239 | | 382 | |
| Interest | 86 | 71 | | 109 | | 58 | |
| PBT | 4,239 | 5,000 | -15% | 4,262 | -1% | 3,766 | 13% |
| Tax | 1,390 | 1,497 | | 1,273 | | 1,178 | |
| PAT (post exceptionals) | 2,850 | 3,503 | -19% | 2,989 | -5% | 2,589 | 10% |
| Minority | 98 | 100 | | 106 | | 78 | |
| Net income | 2,752 | 3,403 | -19% | 2,884 | -5% | 2,511 | 10% |

| Margins | 1QFY14 Actual | 1QFY14 GSe | var bp | 1QFY13 Actual | yoy bp | 4QFY13 Actual | qoq bp |
|----------|------------------|---------------|-----------|------------------|-----------|------------------|-----------|
| Gross | 43.5% | 44.5% | (95) | 41.9% | 164 | 43.5% | 4 |
| EBITDA | 17.3% | 18.9% | (154) | 17.6% | (25) | 14.5% | 286 |
| EBIT | 15.2% | 17.1% | (192) | 16.3% | (106) | 12.7% | 253 |
| Tax rate | 32.8% | 29.9% | 284 | 29.9% | 292 | 31.3% | 152 |

Source: Company data, Goldman Sachs Research estimates

Exhibit 2: Volume growth was strong against a lower base
Quarterly volume growth trajectory



Source: Company data, Goldman Sachs Research estimates

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Reg AC

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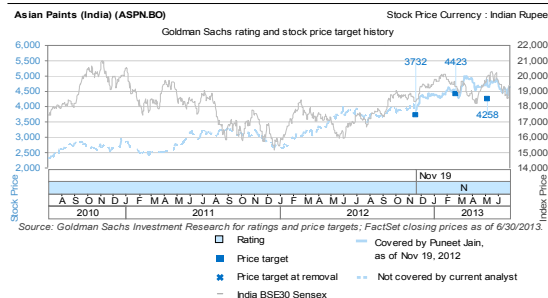
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|--------|---------------------|------|------|----------------------------------|------|------|
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