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## SRF: Robust growth in specialty chemicals biz yields good crop for now

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Patience pays. Investors who held on to the SRF Ltd stock, despite the delayed recovery in its key specialty chemicals business vertical, have been handsomely rewarded. The shares, which had gained less than 1% in 2018, have surged 49% so far this calendar year.

The chemicals business segment has performed strongly in recent quarters, lifting overall earnings of the company.

Revenues and net profit surged 35% and 39%, respectively, in FY19. The performance was boosted by the chemicals and packaging films divisions, which posted 48-51% revenue growth.

Both chemicals and packaging films divisions saw capacity expansion. However, given the excess capacities in the packaging films sector and pressure on profitability, the focus is on chemicals, which is seeing a cyclical recovery.

The backward integration and wide product portfolio in the fluorochemicals space is giving SRF a competitive advantage. Similarly, the reduction in global inventories in the agrochemicals industry is driving new orders for the specialty chemicals division.

Further, the new capacities have come on stream at an opportune time. Cost pressures and consolidation among global agrochemical companies is yielding new business opportunities for custom producers such as SRF and PI Industries Ltd. PI Industries expects the strong growth in

exports to continue in FY20, thanks to new capacities and commercialization of new molecules.

A similar story is playing out at SRF's chemicals division. In its recent interactions with analysts, the management exuded confidence in maintaining its growth momentum, aided by new capacities and orders.

"Increased enquiries from global agro-innovators after a long time give us confidence on robust growth in the specialty chemical business. Higher utilization should bring better economies of scale, leading to higher margins," Emkay Global Financial Services Ltd said in a note on SRF.

With the SRF stock reflecting much of this optimism, valuations are making some analysts wary. Though the long-term story remains intact, a sharp run-up in the stock limits significant upside, Sharekhan Ltd said in a note. The stock is trading at 16 times FY21 earnings estimates, which is not cheap.

However, investors would do well to keep a track on global developments. Even as global agrochemical companies are stepping up purchases, news on the demand and consumption side is not encouraging. Relentless rainfall and flooding have delayed crop sowing in the US. Breakout of the African swine fever is weighing on soya bean usage.

This disruption is pushing up crop prices for now. But coupled with African swine fever and global trade tensions, demand can potentially get affected, weakening the recovery in the sector. This is the key risk investors need to watch out for.

**The backward integration, wide product portfolio in fluorochemicals are giving SRF a competitive advantage**