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Journalist: Ram Prasad Sahu

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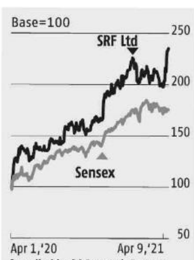
Hike in chemicals prices, higher demand to support SRF stock

Medium-term prospects remain strong, but upside limited following recent rally



Compiled by BS Research Bureau

RAM PRASAD SAHU

Shares of India's largest specialty chemicals company SRF hit their all-time highs on Thursday, on expectations of strong March quarter (Q4) results, higher realisations from price hikes, and ongoing expansion, which should help sustain revenue growth. The stock, which has nearly doubled in value over the last year, is also a candidate for inclusion in the MSCI Standard index in the upcoming semi-annual review in May.

Higher prices of chemicals on account of supply disruptions and end-user demand is a positive for the specialty chemicals and packaging segments. Rohit Sinha of Emkay Research expects the increasing need for hygienic food and pharmaceutical packaging to support demand for SRF's BoPET (biaxially-oriented polyethylene terephthalate) and (biaxially-oriented polypropylene) products. This should also help mitigate the impact of rising PET prices.

In the refrigerant gas segment, the automotive recovery has been encouraging and should support volumes in the domestic market. The prices of refrigerant gases (R-22) increased in Q4 and could help margins.

Sales growth in packaging and chemicals (40 per cent contribution each to overall revenues) should help the company post 20 per cent year-on-year (YoY) revenue growth in the quarter. Analysts at Sharekhan expect margins to improve by 394 basis points YoY to 24.9 per cent, aided by healthy spread for packaging films and price hike for specialty chemicals.

There are multiple triggers and favourable tailwinds for the company going ahead. Analysts at Investec Securities believe that the rising use of halogens in agrochem and pharma molecules, China+1 sourcing strategy and higher outsourcing are positive for the company.

Moreover, higher capital expenditure allocation of ₹3,500 crore over the next two years towards the specialty chemicals space would be beneficial for overall growth. While the company is expected to grow at 19 per cent in the FY21-23, revenue and operating profit growth for specialty chemicals is pegged at 25-30 per cent.

While medium-term prospects are strong and revenue/net profit growth is pegged to grow at 19 per cent each in the FY21-23 period, the stock, which has risen 10 per cent over the last four trading sessions, factors in these gains. Given the limited upside from current levels, investors should await a price correction to accumulate the stock.