

Rashtriya Chemicals & Fertilisers

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The Government of India is divesting 68,961,012 shares (12.5% stake) in Rashtriya Chemicals & Fertilisers (RCF) out of its shareholding of 92.5% in the domestic market through Offer for Sale (OFS). **We recommend investors to SUBSCRIBE the RCF issue.**

Investment Arguments

New Urea Investment Policy to boost expansion plan

The recently approved New Urea Policy is likely to encourage fertilizer companies to set up new plants and expand existing capacities, thereby reducing dependence on imports. India currently imports ~30% of its urea requirement. The new policy provides moderate upside to companies as the government plans to give 12-20% post-tax returns (earlier, returns were less than 12%) on fresh capital infused by manufacturers for both - setting new urea plants, and for the expansion or modernisation of the existing plants. The government plans to facilitate this by providing subsidy on gas prices (the main feedstock of urea, accounting for ~80% of the cost) subject to its price remaining at or below the level of US\$14/mmbtu.

The company is geared up with a capacity expansion plan of urea at Thal by 12.7lakh MT p.a. to be completed in the next three years with a capex of ~₹4,112cr, which the company plans to fund through a mix of equity, debt and internal funding. The project has been cleared by pre-Public Investment Board (PIB) and the company is now seeking PIB's and CCEA's approval.

Great distribution network and high brand recall

RCF has ~6,314 dealers across the country as well as over 500 co-operative marketing societies that facilitate its pan-India reach. The company enjoys a high brand recall with brands like *Ujjwala* (urea); *Suphala 15:15:15* and *Suphala 20:20:20* (NPK); *Biola* (bio-fertilizers); *Microla* (micro nutrients) and *Sujala* (water soluble fertilizers). Further, given the high brand recall, RCF enjoys a market share of 10.7% in the urea market, 5.5% in the NPK market and 7.3% in the MOP market.

Projects under consideration may provide upside in future

In addition to the expansion plan at the Thal unit, the company is working on other projects for capacity expansion, which are also expected to be completed in a span of next three to four years. These include –

- 1) Coal gasification based fertilizer & chemical complex at Talcher (12.7lakh MT urea, 3.3lakh MT ammonium nitrate and 2.8lakh MT nitric acid) on a JV basis with Coal India and Fertilizer Corporation, with a capex of ~₹9,126cr.
- 2) Fertilizer project in Ghana (12.7lakh MT urea) on a JV basis with a capex of ~₹7,121cr.
- 3) Granulated Single Super Phosphate project at Thal with a capex of ~₹307cr.

However, none of these projects are near their zero dates, while they also have a long gestation period.

SUBSCRIBE

CMP	₹44
OFS floor price	₹45

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Company overview

RCF is a Miniratna PSU incorporated in 1978 as a chemical manufacturer. The Government of India's shareholding in the company stands at 92.5%. RCF is in the business of manufacturing and marketing of various fertilizers and chemicals and is among the leading players in its industry segment. Its products enjoy high brand recall. It is the fourth largest producer of urea (sold under the brand name *Ujjwala*) with a market share of 10.7% and total capacity of ~23lakh MT p.a. in India. The company has two operating units at Trombay and Thal in Maharashtra. RCF has expanded its revenue stream and product portfolio through sale of imported diammonium phosphate (DAP) and muriate of potash (MOP).

Exhibit 1: Business Structure

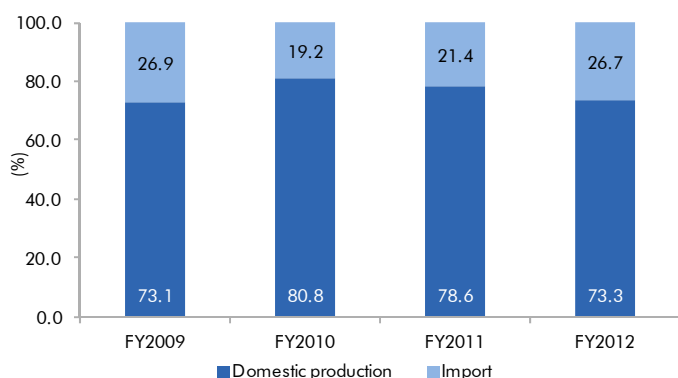
Segments	Products	Sales*	EBITDA*
Nitrogenous Fertilizers	Urea - Manufactured & Imported	50%	
P&K Fertilizers	Complex Fertilizers		
	– Suphala 15:15:15	36%	62%
	– ANP 20:20:0		
	– DAP, MOP, Complexes Imported		
Industrial Chemicals	Used in various Industries like Pharmaceuticals, Drugs, dyes, pesticides etc	13%	
Specialty Nutrients	Bio Fertilizers		38%
	Micro Nutrients	1%	
	Water Soluble Fertilizers		

Source: Company Presentation, Angel Research, *contribution in FY2012

Industry

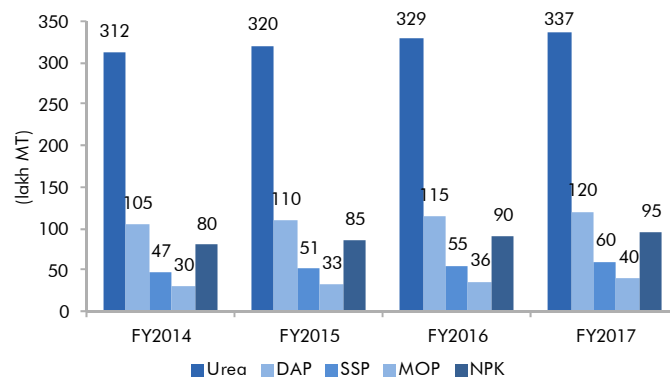
The Indian fertilizer industry is one of the most regulated sectors in the country. The urea sector (which accounts for around 50% of the fertilizer consumption) is completely regulated where retail prices are fixed and subsidy is variable in order to ensure cost plus return (12% post tax RoE). On the contrary, the non-urea sector (DAP and NPK fertilizers) functions under a fixed subsidy. A variable retail price framework is followed with considerable pricing freedom being granted since April 2011.

Exhibit 2: Demand fulfilment – Domestic vs. imports



Source: Company, Angel Research

Exhibit 3: Fertilizer demand forecasts in India



Source: Company, Angel Research

The growth in overall demand for fertilizers has remained at ~5% over the period FY2005-12. However, the production has remained largely stagnant during the same period, mainly because of lack of capacity addition due to various policy related issues and limited availability of raw materials. Hence, India's dependence on fertilizer imports has increased to the current level of ~27% for urea and 68% for DAP.

However, with the New Urea Policy coming in, we expect the scenario to improve and dependence on imports to reduce in coming years.

Exhibit 4: Major players producing Urea in India

Company	Urea Capacity* (lakh MT)	Other Products
IFFCO	42.4	NPK, DAP, Phosphates, Complex
NFL	32.3	-
KRIBHCO	25.9	-
RCF	23.3	Nitro Phosphate, Ammonium Nitrate Phosphate
Chambal Fertilizers & Chemicals Ltd.	17.3	-
Nagarjuna Fertilizers & Chemicals Ltd.	15.2	-

Source: Company, Angel Research, * as on November 2012

Risks and concerns

- Fluctuations in global raw material & natural gas prices
- Policy related issues and stringent terms in gas supply and transportation contracts and their operability
- Adverse movements in exchange rate
- Adverse agro-climatic conditions may impact the performance of the company
- Recession in international chemical market leading to un-remunerative domestic prices

Outlook and valuation

The new urea investment policy and capacity expansion plans provide the company a healthy outlook but being a public sector company in a highly regulated industry, the implementation of projects as well as the policies might get delayed, which may pose a risk to the company's future.

The company has fixed a floor price of ₹45, which is at a premium of 2.6% from its current market price (CMP) ₹44. At the CMP, the stock is trading at a PE of 8.7x on TTM basis and at the floor price of the issue of ₹45, it is trading at 9.0x on TTM basis. **We recommend investors to SUBSCRIBE the RCF issue as it is fairly valued and the successful completion of projects in pipeline will provide upside to the stock in the future.**

Profit and Loss Statement

Y/E March (₹ cr)	FY2008*	FY2009*	FY2010	FY2011	FY2012
Total operating income	5,141	8,366	5,642	5,524	6,434
% chg		62.8	(32.6)	(2.1)	16.5
Net Raw Materials	2,399	5,099	3,651	2,937	3,497
% chg		112.6	(28.4)	(19.5)	19.0
Other Mfg costs	1,312	1,369	552	925	1,011
% chg		4.3	(59.7)	67.6	9.3
Personnel	236	382	359	400	424
% chg		61.7	(6.2)	11.6	5.9
Other	902	1,113	740	861	1,102
% chg		23.4	(33.5)	16.4	28.0
Total Expenditure	4,850	7,963	5,302	5,124	6,034
EBITDA	291	403	340	400	399
% chg		38.5	(15.6)	17.6	(0.1)
(% of Net Sales)	5.7	4.8	6.0	7.2	6.2
Depreciation & Amortisation	83	87	106	113	143
EBIT	208	316	234	287	257
% chg		52.2	(25.9)	22.5	(10.6)
(% of Net Sales)	4.0	3.8	4.2	5.2	4.0
Interest & other Charges	66	111	71	69	49
Other Income	100	119	180	137	167
(% of Net Sales)	2.0	1.4	3.2	2.5	2.6
Recurring PBT	142	206	164	218	207
% chg		45.3	(20.3)	32.8	(4.7)
PBT (reported)	242	325	344	354	374
Tax	84	114	109	110	125
(% of PBT)	34.7	35.2	31.8	30.9	33.5
PAT (reported)	158	211	234	245	249
Extraordinary Expense/(Inc.)	(1)	-	-	(1)	(1)
ADJ. PAT	159	211	234	246	250
% chg		32.7	11.3	4.9	1.8
(% of Net Sales)	3.1	2.5	4.2	4.4	3.9
Basic EPS (₹)	2.9	3.8	4.2	4.5	4.5
Fully Diluted EPS (₹)	2.9	3.8	4.2	4.5	4.5
% chg		32.7	11.3	4.9	1.8

Note: *Standalone

Balance Sheet Statement

Y/E March (₹ cr)	FY2008*	FY2009*	FY2010	FY2011	FY2012
SOURCES OF FUNDS					
Equity Share Capital	552	552	552	552	552
Reserves & Surplus	987	1,120	1,284	1,460	1,620
Shareholder's Funds	1,539	1,672	1,836	2,012	2,171
Total Loans	1,243	1,425	1,355	422	1,185
Other Long Term Liabilities	0	0	-	85	72
Long Term Provisions	0	0	-	108	127
Deferred Tax (Net)	166	149	164	156	214
Total Liabilities	2,948	3,245	3,354	2,783	3,770
APPLICATION OF FUNDS					
Gross Block	2,778	2,875	3,116	3,264	3,521
Less: Acc. Depreciation	1,693	1,762	1,867	1,980	2,123
Less: Impairment	31	31	1	1	1
Net Block	1,054	1,082	1,247	1,282	1,397
Capital Work-in-Progress	115	248	178	82	177
Lease adjustment	0	-	-	-	-
Goodwill	0	-	-	-	-
Investments	360	20	0	15	18
Long Term Loans and advances	0	0	-	98	136
Other Non-current asset	0	0	-	14	16
Current Assets	2,290	3,819	2,883	2,257	3,874
Cash	49	412	785	419	592
Loans & Advances	231	926	830	88	85
Inventory	872	693	410	535	1,178
Debtors	1,138	1,788	859	857	1,978
Other current assets			-	357	41
Current liabilities	872	1,925	954	966	1,848
Net Current Assets	1,418	1,894	1,929	1,291	2,026
Misc. Exp. not written off	2	1	-	-	-
Total Assets	2,948	3,245	3,354	2,783	3,770

Note: *Standalone

Cash Flow Statement

Y/E March (₹ cr)	FY2008*	FY2009*	FY2010	FY2011	FY2012
Profit before tax	242	325	344	354	374
Depreciation	83	87	106	113	143
Change in Working Capital	(166)	(113)	338	273	(562)
Direct taxes paid	(84)	(114)	(109)	(110)	(125)
Others	62	84	(38)	25	20
Cash Flow from Operations	138	269	640	656	(150)
(Inc.)/Dec. in Fixed Assets	(115)	(230)	(170)	(53)	(353)
(Inc.)/Dec. in Investments	(360)	340	20	(15)	(3)
(Incr)/Decr In LT loans & adv.			-	(112)	(39)
Others	3	20	52	116	98
Cash Flow from Investing	(472)	130	(99)	(64)	(296)
Issue of Equity	0	-	-	-	-
Inc./(Dec.) in loans	288	181	(69)	(933)	763
Dividend Paid (Incl. Tax)	(5)	(5)	(7)	(8)	(8)
Others	(130)	(211)	(92)	(16)	(136)
Cash Flow from Financing	153	(36)	(168)	(957)	619
Inc./(Dec.) in Cash	(181)	363	372	(365)	173
Opening Cash balances	231	49	412	785	419
Closing Cash balances	49	412	785	419	592

Note: *Standalone

Key Ratios

Y/E March	FY2008*	FY2009*	FY2010	FY2011	FY2012
Valuation Ratio (x)					
P/E (on FDEPS)	15.2	11.5	10.3	9.8	9.7
P/CEPS	10.0	8.1	7.1	6.7	6.2
P/BV	1.6	1.4	1.3	1.2	1.1
EV/Net sales	0.6	0.4	0.5	0.4	0.5
EV/EBITDA	11.2	8.5	8.8	6.0	7.5
EV / Total Assets	1.2	1.1	0.9	0.9	0.8
Per Share Data (₹)					
EPS (Basic)	2.9	3.8	4.2	4.5	4.5
EPS (fully diluted)	2.9	3.8	4.2	4.5	4.5
Cash EPS	4.4	5.4	6.2	6.5	7.1
DPS	0.1	0.1	0.1	0.1	0.1
Book Value	27.9	30.3	33.3	36.5	39.4
DuPont Analysis					
EBIT margin	4.0	3.8	4.2	5.2	4.0
Tax retention ratio	0.7	0.6	0.7	0.7	0.7
Asset turnover (x)	2.3	3.5	2.5	2.6	2.3
ROIC (Post-tax)	6.0	8.5	7.2	9.4	6.2
Cost of Debt (Post Tax)	3.9	5.4	3.5	5.4	4.1
Leverage (x)	0.5	0.6	0.3	(0.0)	0.3
Operating ROE	7.1	10.3	8.3	9.4	6.7
Returns (%)					
ROCE (Pre-tax)	7.5	10.2	7.3	10.9	7.2
Angel ROIC (Pre-tax)	9.2	13.1	10.5	13.6	9.3
ROE	10.6	13.1	13.4	12.8	12.0
Turnover ratios (x)					
Asset TO (Gross Block)	1.9	3.0	1.9	1.7	1.9
Inventory / Net sales (days)	57	34	36	31	49
Receivables (days)	72	64	86	57	80
Payables (days)	-	64	99	68	85
WC cycle (ex-cash) (days)	97	65	74	58	81
Solvency ratios (x)					
Net debt to equity	0.5	0.6	0.3	(0.0)	0.3
Net debt to EBITDA	2.9	2.5	1.7	(0.0)	1.4
Int. Coverage (EBIT/ Int.)	3.1	2.9	3.3	4.1	5.2

Note: *Standalone

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