



**Poddar Pigments (NSE Code: PODDARMENT) – Alpha/Alpha + stock
report for Jan'17**

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Company Snapshot (26th Jan'17)

Rating – Positive – 3% weightage; this is not an investment advice (refer rating interpretation), the rating is only for indicative purpose and please take your own decision regarding the same.

CMP – 226.05 (BSE); 227.95 (NSE)

Dividend yield – 1.10%

BSE Code – 524570; **NSE Code** – PODDARMENT

Market capitalization – Rs 240.00 cr.

Total Equity shares – 1.06 cr.

Face Value – Rs 10.00

52 Weeks High/Low – Rs 274.70/120.70

Particulars (in cr.)	FY 09	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
Total Sales from operations	119.73	153.09	186.48	221.91	275.55	313.23	318.31	325.99
Total Cost of goods sold	90.43	117.65	145.87	172.89	221.18	252.47	253.72	254.19
Gross Profit	29.3	35.44	40.61	49.02	54.37	60.76	64.59	71.8
Gross Profit margin (%)	24.47%	23.15%	21.78%	22.09%	19.73%	19.40%	20.29%	22.03%
EBITDA	8.52	11.63	15.6	19.73	20.02	22.14	22.43	23.63
EBITDA margin (%)	7.12%	7.60%	8.37%	8.89%	7.27%	7.07%	7.05%	7.25%
Other Income								
Interest and other income	0.83	0.89	0.71	0.71	0.78	1.17	1.43	2.41
Exchange gain/loss	0	0.84	1.80	0.42	1.15	0.57	1.51	2.12
Depreciation	-2.16	-2.15	-2.33	-2.7	-2.65	-2.60	-2.85	-2.62
Interest Cost	-1.22	-0.61	-1.78	-1.79	-1.69	-1.21	-0.59	-0.43
PBT	5.97	10.60	14.00	16.37	17.61	20.07	21.93	25.10
PBT after exceptional items		17.16		14.42	17.53			
PAT	3.97	14.19	9.55	9.84	12.79	13.47	16.31	18.34
ROAE	10.97%	33.43%	19.06%	17.21%	19.38%	17.61%	18.48%	17.94%
Cash Flows from operations	6.51	6.59	2.03	18.71	9.76	13.98	19.33	4.40
Net Debt	5.45	1.75	17.36	15.82	11.01	1.46	-13.09	-11.75
Net Debt to equity ratio	0.14	0.04	0.32	0.26	0.15	0.02	-0.14	0.00

Introduction

Promoted by Mr. S. S. Poddar, Poddar Pigments (PPL) is an ISO 9001:2008 QMS certified company and manufactures colour and additive masterbatches for the dope dyeing of the man-made fibres (MMF), various plastic applications and engineering plastics and compounds.

As per the company, it has the unique distinction of being the first company in India to manufacture Masterbatches for the dope-dyeing of Polypropylene, Nylon & Polyester Multifilament Yarn/ Fibres.

We like the company on several fronts including its consistency in performance over the years, the way it has managed its balance sheet with minimal debt, strong tailwinds for the masterbatch sector, high promoter holding and reasonable valuations.

One concern that we have right now is that company seems to be operating near full capacity, however what is good is that the business is not very fixed capital intensive and therefore expanding capacity shouldn't be an issue.

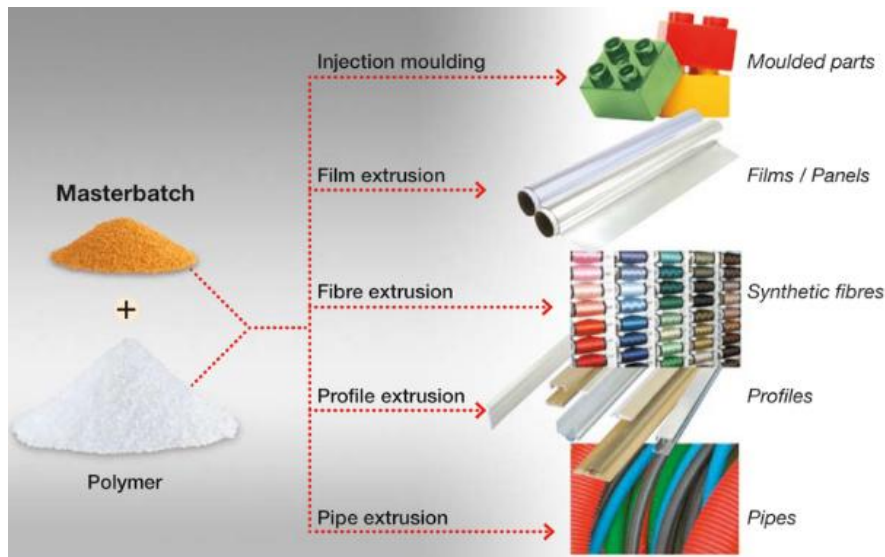
Understanding Business and Company

Masterbatch is basically a solid or liquid additive used for colouring (colour masterbatch) or imparting other properties to plastics (additive masterbatch) and man-made fibres.

In other words – Polymer granulates with a high percentage of additives, higher than in the end use, are called masterbatch. In later production steps, such as injection moulding, film or fibre production, those granulates are mixed with the raw polymer for colouring or the targeted modification of certain properties.

Advantages of Masterbatch – In comparison to pastes, powders or fluid additives, using masterbatch increases the process stability. The reason lies in the exactly defined pigment quantity in each granulate. The goal of masterbatch production is the ideal dispersion of additives in the polymer matrix. The fine, powdery feed material often tends to

agglomerate and therefore is difficult to work with. Masterbatches with an additive share of 20 – 90% are available, depending on the feed material. Some of the masterbatch applications are pictured below:-



Source: adroitflowcontrol.in

Generally, there are three masterbatch groups –

1. Colour masterbatch, which is used for colouring plastics products
2. Additive masterbatch, which provides for certain chemical and physical properties of the end product (for example UV stabilizers, flame retardants, anti-static or anti-block agents)
3. Filler masterbatch, that is filled with a high share of fillers like chalk

So, as mentioned above, Poddar Pigments manufactures colour and additive masterbatches for man-made fibres, plastic applications and engineering plastics and compounds.

The company has its manufacturing facility at Jaipur and it has the capacity to manufacture 14,000 tonnes of specialty masterbatches per annum. It started with the capacity of 1200 MTPA in 1991.

The company supplies masterbatches for the following segments:

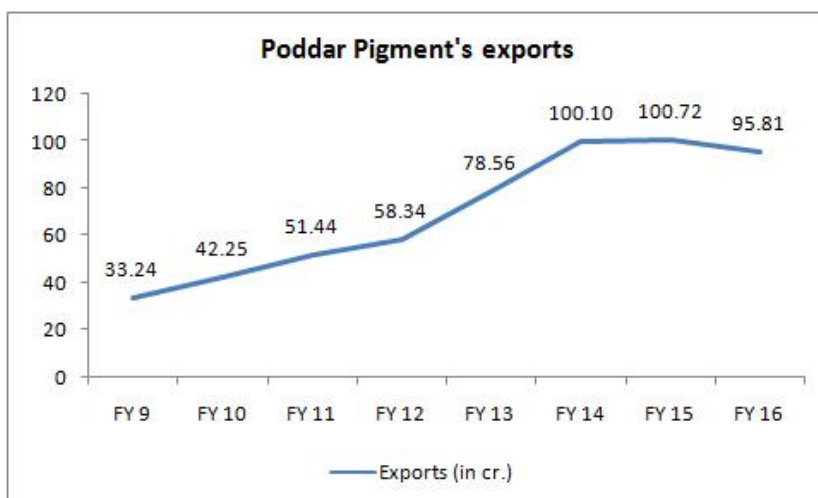
Man-made fibres – In the man-made fibres segment the company supplies masterbatches for Polyester, Polypropylene and Polyamide.

The company provides wide range of masterbatches which are used in textile processes and their applications include textile, home furnishing, automotive, upholstery, luggage, lamination fabrics etc.

Plastics and Packaging – Apart from the White, Black and Colour masterbatches PPL also manufactures various high purity additive masterbatches available in LDPE, PP & PET base polymers for various plastics applications viz. PE, PP & PET films, Injection & Blow moulding, PP Spun Bonded Non-woven fabrics, PET Bottles, Cables, Irrigation pipes, plumbing pipes, etc

Engineering Compounds – The Company also offers product range under MASTERPLUS Engineering Plastic Compounds. These masterbatches are used in various products ranging from electrical switches and other electrical components, Home Appliances, Automotives, and Telecommunication devices, etc.

Exports – The Company exports to a large number of countries worldwide and has a strong foothold in the global market. Share of exports to total net sales has consistently remained above 25% since the last many years.

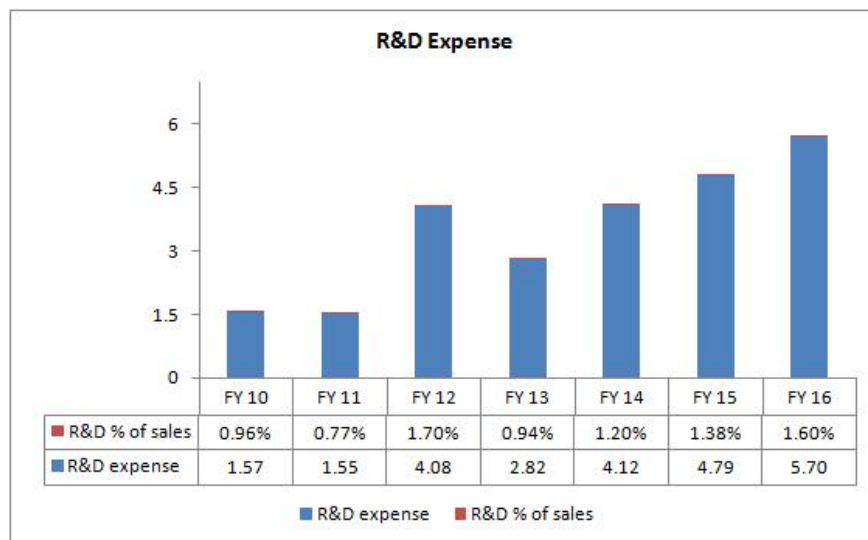


Source: Poddar Pigment's ARs

Barring last 2 years when the exports sales remained stagnant, the company recorded 25% CAGR in exports from FY 09 to FY 14.

Going forward management intends to make further inroads into other markets by participating in various international events, like it did in 2015 by participating in ITMA held in Milan, Italy.

Research and Development – Over the years the company has invested significantly in its R&D facility and its in-house R&D facility is recognized by the Department of Science and Industrial Research (DSIR).



Source: Poddar Pigment's ARs

By investing in R&D the company intends to continuously pursue the development of new and innovative products to stay ahead of the competition and take away market share from other organized and unorganized players.

Masterbatch industry overview

The masterbatch industry can be broadly classified into three sectors: organized, medium and small. A substantial part of the market is catered to by the small sector, comprising

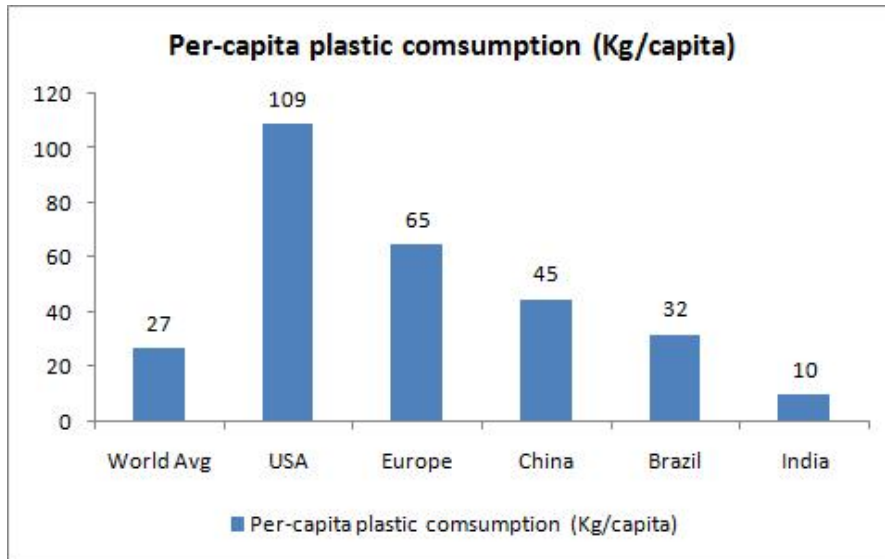
largely of small manufacturing units spread throughout the country. These units mostly cater to their respective local markets. The medium sector is relatively small in size, though it caters to a larger market. The organized sector comprises of select players and caters to the organized and quality conscious market. It appears that the organized sector is taking over the market share from the small and medium sector by meeting the stringent quality requirements, timely deliveries, prompt technical services and R&D backup.

The growth of masterbatch industry is totally reliant on the growth in the consumption of plastic/polymer products and synthetic textiles by end users in the Indian and international market.

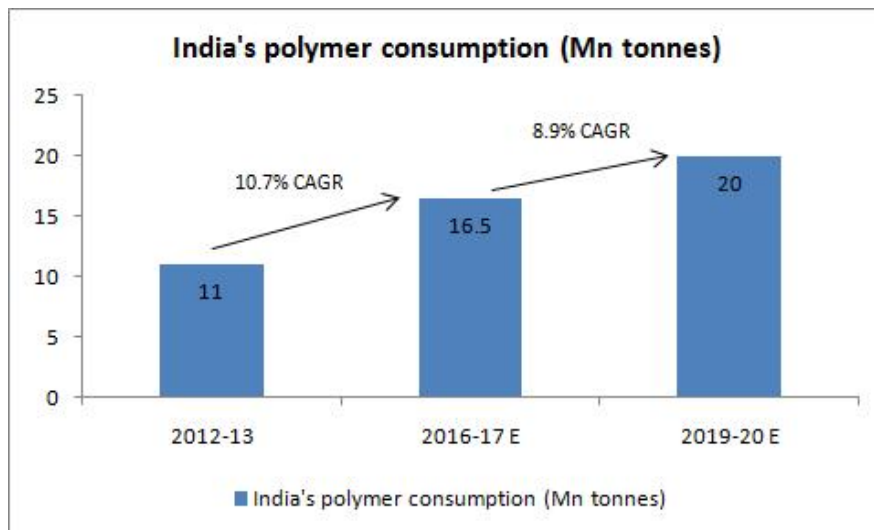
Plastics are rapidly replacing items like wood, steel, rubber etc. Demand is increasing for high performance plastics in major end – user industries like agriculture, packaging, automobile, consumer durables, telecom, etc. With the development of bio-additives, usage of masterbatches holds positive prospects for the manufacturing of bio-degradable plastics. Other important innovations such as development of anti-microbial masterbatches, flame retardant masterbatches, antioxidant masterbatches is set to drive the market for masterbatches across various end user industries.

Similarly, with the rising cost of natural and blended textiles, demand for synthetic textiles is bound to increase. While the global per capita consumption of man-made fibres (MMF) is around 12 kg per annum, it is merely 3.5 kg in India, providing significant scope for the increase in domestic consumption.

As per the report by Tata Strategic, India's per capita consumption of plastic products is ~10 kg against 32 kg in Brazil, 45 kg in China, 65 kg in Europe and 109 kg in US. Current low per capita consumption level of plastic products as compared to developed countries per capita consumption suggests that India offers a huge opportunity over long term.

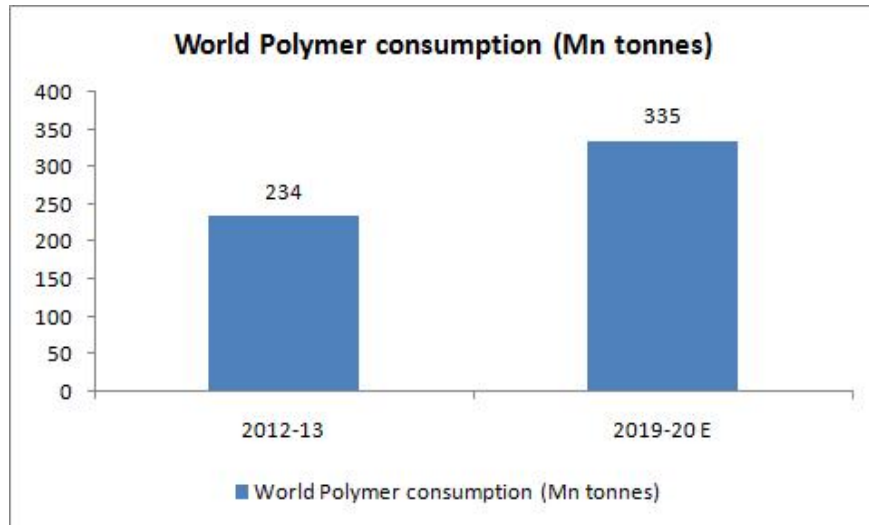


Source: FICCI, Tata Strategic report



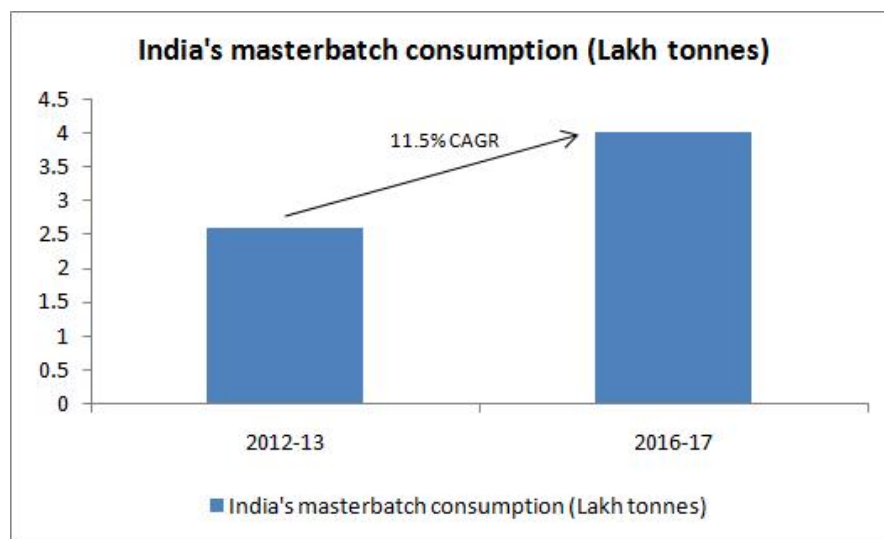
Source: FICCI

Polymer consumption in India as of FY 13 stood at 11 MMTPA and is expected to grow at CAGR of 9% to 20 MMTPA by FY 20.



Source: ABM research

As of FY 13, global polymer consumption stood at ~234 MMTPA and is likely to grow at CAGR of 5.3% to 335 MMTPA by FY 20. This shows that globally as well opportunity for masterbatch industry is very huge and Indian players can capitalize on the same.



Source: Company, ABM research

Masterbatch consumption in India is estimated to be 4 lakh tonnes in 2016-17 from 2.6 lakh tonnes during the year 2012-13 and thereby the overall industry is expected to continue reporting 11-12% growth.

We believe the next leg of growth for organized players like Poddar Pigments will come from the fact that unorganized market is still more than 50% of the overall masterbatch industry. As per industry estimates, India's masterbatch industry is currently valued at Rs 5000 crore and the organized players account for ~ 50% of the market size. Industry is largely fragmented in nature with Plastiblends being the market leader.

Promoters/Management

Poddar Pigments is an owner operated business with Mr. S. S. Poddar at the helm of the affairs of the company as the promoter and the Managing Director.

He is ably supported by Mr. R. K. Sureka who is the CEO of the company. Mr. Sureka has been working with the company for more than 19 years now.

In small cap companies, we believe it's important as an investor that the promoters hold reasonably high stake and in the case of Poddar Pigments the promoters own more than 60% stake in the company.

Overall we find the promoters to be conservative and they have managed the operations very efficiently. Since FY 11 they have been continuously paying dividend and have also managed to reduce debt.

We have also not come across any major red flags in terms of related party transactions.

Shareholding pattern (as reported on BSE)

	Dec'16	Sep'16	Jun'16
Promoter and Promoter Group	60.85%	60.85%	60.85%
India	60.85%	60.85%	60.85%
Foreign			
Public	39.15%	39.15%	39.15%
Total	1,06,10,000	1,06,10,000	1,06,10,000

As per the latest shareholding records, Promoters own 60.85% stake in the company which is reasonably high and aligns the interests of those running the company in line with minority shareholders.

It's important to note that in the last more than 10 years Poddar Pigments hasn't diluted equity and in fact bought back 15.90 lakh shares in FY 10.

As on 31st Dec'16, the major shareholders of the company and their stakes are as below:

Name of the shareholder	Category	% stake in Poddar Pigments
Promoters and PAC	Promoters	60.85%
Mayuka Investment Ltd	Public	2.17%
Pramila Maheshkumar Bang	Public	2.16%
Himshikhar Investment	Public	1.92%
Bang Purnima Mahesh	Public	1.72%
Subramanian P	Public	1.31%

Poddar Pigments – Performance Snapshot

One of the major positives of Poddar Pigments is its operating performance which has been very consistent over the years.

Particulars (in cr.)	FY 09	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
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Depreciation	-2.16	-2.15	-2.33	-2.7	-2.65	-2.60	-2.85	-2.62
Interest Cost	-1.22	-0.61	-1.78	-1.79	-1.69	-1.21	-0.59	-0.43
PBT	5.97	10.60	14.00	16.37	17.61	20.07	21.93	25.10
PBT after exceptional items		17.16		14.42	17.53			
PAT	3.97	14.19	9.55	9.84	12.79	13.47	16.31	18.34
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Net Debt	5.45	1.75	17.36	15.82	11.01	1.46	-13.09	-11.75
Net Debt to equity ratio	0.14	0.04	0.32	0.26	0.15	0.02	-0.14	0.00

Source: Poddar Pigment's ARs

We believe, if both the business and the management are good it should reflect in the operating and financial performance of the company. If the financial performance has consistently been poor with no visible signs of improvement, then either the business or the management or rather both are not good.

As far as Poddar Pigments is concerned, over the years it has shown good consistency in operations. Barring last 2 years the company has consistently reported ~20% growth in

sales on year on year basis. Even during FY 16 the company reported 8% growth in productivity, however overall sales growth was only 3% on account of 15-20% dip in commodity prices.

For companies not dealing in branded products (read: pricing power) we like to check gross margins to see if the company can withstand volatility in raw material prices without getting impacted much. Poddar Pigments has performed reasonably well on that front as it has been able to maintain its gross margins in the range of 20-22% on a very consistent basis. While the gross margins have been consistent, we believe there's scope for improvement as the industry leader Plastiblends commands around 28-30% gross margins.

Further, there's been improvement in terms of operating efficiency with the EBITDA margins of the company improving from 3-4% (back in 2005-2007) to current levels of 7-8%.

Despite increase in scale of operations, company's depreciation and interest costs haven't increased much over the years. The business is low on fixed capital intensity and therefore capital expenditures have been low.

Important Numbers	FY 9	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
Inventory Days	52	47	58	49	47	44	45	42
Debtor Days	57	46	50	47	52	49	39	57
Cash Flows from operations	6.51	6.59	2.03	18.71	9.76	13.98	19.33	4.40
ROAE%	10.97%	33.43%	19.06%	17.21%	19.38%	17.61%	18.48%	17.94%
Debt to equity ratio	0.14	0.04	0.32	0.26	0.15	0.02	-0.14	0.00
Net Debt	5.45	1.75	17.36	15.82	11.01	1.46	-13.09	-11.75

Source: Poddar Pigment's ARs

Company has also done extremely well in terms of working capital management and as a result its cash flows from operations have consistently been good and more or less in line with reported profits.

As can be seen from the above illustration the average number of inventory days for FY13-FY16 period has reduced to 44 against 52 for FY09-FY12. Similarly, debtor days have reduced to 49 from 50 for the above mentioned periods.

Thus, with very low CAPEX and efficient working capital management, the company is now debt free and has surplus funds to the tune of around 10 crores.

As far as return ratios are concerned, the company has consistently been recording ROE and ROCE in excess of 17%.

On the growth front, the last two years saw lower growth in sales on account of slowdown in exports market and lower raw material prices which impacted value growth. We believe, going forward growth rates may improve with the improvement in demand in both domestic and exports market and also the fact that commodity prices seem to have bottomed out and have started increasing.

Increasing capacity should not be much of a concern, because in general the CAPEX involved is small and can be managed by internal accruals or through minimal debt. Further, in the past company has managed to exceed 100% of the rated capacity utilization.

Valuations

At around current price of 227 the market capitalization of the company is Rs 240 crores and the enterprise value is ~ Rs 230 crores. The enterprise value is lower than market cap as the company is cash rich with surplus of around 10-12 crores as of 30th Sep'16.

For the trailing twelve months the stock has recorded PAT of Rs 20.69 crores and EBIT of Rs 25.88 crores. The stock is therefore trading at 11.60 times trailing twelve months earnings and EV/EBIT multiple of 8.88.

We believe the current valuations on absolute basis are reasonable; further we believe the element of cyclicity in the business has been very low with operating margins being consistently maintained in the range of 7-8% and steady increase in sales. As mentioned

above, going forward we expect improvement in sales on the back of both increase in commodity prices and overall improvement in demand.

In the masterbatches segment, Plastiblends is another major listed company and currently quoting at 18 times trailing twelve months earnings.

Dividend Policy

Dividend Payout ratio					
	FY 12	FY 13	FY 14	FY 15	FY 16
Dividend Payout ratio	21.54%	16.58%	17.74%	16.25%	14.45%

Poddar Pigments has been consistently paying dividends since FY 11 and prior to that in FY 10 it bought back 15.90 lakh shares of the company.

While there's no absolute stated dividend policy, since the last few years the dividend payout ratio has been in the range of 15-20% which we believe is reasonable considering company might have to expand capacity in near future.

Company holds some direct equity investments; however the amount involved is small and the major investments are in liquid funds.

Risks & Concerns

Slowdown in end user industries can impact the demand for masterbatches and thereby the growth of Poddar Pigments.

Besides domestic sales, Poddar Pigments also derives around 30% of its sales from exports and thereby currency fluctuations can impact the profitability of the company.

Till now company has shown good resilience in terms of maintenance of margins, however masterbatches is a very competitive segment and increased competitive intensity can impact company's ability to pass on price hikes in raw material costs.

Company's plants are running close to optimum capacity utilization. If the company fails to expand capacity, its overall growth will be limited and will impact the returns for the shareholders.

Disclosure: I don't have any investment in Poddar Pigments and have not traded in the stock in the last 30 days.

Best Regards,

Ekansh Mittal

Research Analyst

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Rating Interpretation

Positive – Expected return of ~15% + on annualized basis in medium to long term

Neutral – Expected Absolute return in the range of +/- 15%

Negative – Expected Absolute return of over -15%

Coverage closure – No further update on the stock

% weightage – allocation in the subject stock with respect to equity investments

Short term – Less than 1 year

Medium term – Greater than 1 year and less than 3 years

Long term – Greater than 3 years

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Analyst ownership of the stock: No

Details of Associates: Not Applicable

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