

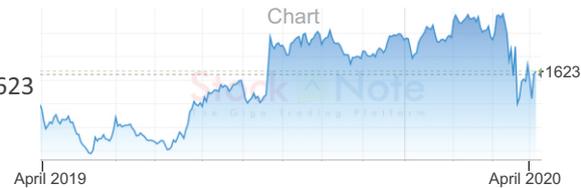
Asian Paints

Quality company in the consumption space which is available at attractive valuations and is capable of tiding through the Covid19 pandemic with minimal headwinds.

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Recommendation : **Accumulate**

Date : 09th April 2020
Current Price Range : Rs 1600 - 1623
Outlook : **Strong Upside**
Investment Period : 5 years



Positives

Long term

Leader in the true sense: Having a 50% market share in the organised space, this company enjoys dominance in the decorative paints segment along with a 20% share in the automotive industrial paints segment.

High Barriers to Entry: Strong distribution network of 60,000+ dealers enable access to the nooks and corners of India. Also, innovative idea of installing tinting machines with dealers, instead of a common warehouse, has enabled to reduce storage space for paints at the dealer's end. This itself becomes a major entry barrier for a new entrant as he has to overcome the resistance of a dealer for yet another tinting machine.

Industry Drivers: 80% demand is from repainting, hence there is limited dependence on new painting. Repainting cycle has shrunk from 7-8 yrs earlier to 5 yrs now which is a big positive. Moreover, house rentals in metropolitan cities aids the demand for paints (Short cycle of 3 yrs). Oligopolistic nature of the industry drives strong pricing power which improves the topline.

The OPEC+ Fail Impact: The sudden slump in crude prices to sub \$30/barrel levels bodes extremely well for this paint player as crude oil derivatives form 30-35% of its raw material costs.

Robust Strategies: Strategizes on pursuing volume growth by pushing products in the lower end of its portfolio and focuses on project sales that carry lower margins. On a 5-year basis over FY14-19, EBITDA margin has expanded mainly due to operating leverage as they reaped scale benefits due to capacity expansion.

Well Managed Books to Accounts: Strong balance sheet with minimum leverage and high free cash flows to sales of 4.44% will enable Asian Paints to tide through the pandemic. Additionally, it has the lowest cash conversion cycle in the industry compared to its competitors. Since the last 5 years, it has maintained an interest coverage ratio of over 50 and an asset turnover ratio of around 1.5.

Risks

Low presence in Industrial segment: The industrial paint category is about 25% of the paint market in India but it only contributes to about 3% of total revenues for the company. Its peers such as Kansai Nerolac and Akzo Nobel have a higher market share in this category.

Raw material price volatility: Raw material costs account for 55% of total cost to the company. Majority of the raw material comprises of crude based derivatives and titanium dioxide. Therefore, profitability and margins fluctuate with the volatility in the raw material prices.

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