

## Consumer Staples & Discretionary

### Worm's world view #18: Conversations with paint dealers

Asian paints have reduced the 'trade scheme' (discounts) to 3-5% from 5-6% earlier. Also earlier the dealers were getting benefits based on actual purchases. Now the scheme is linked to certain targets. We expect dealers to focus more on Asian Paints' products to achieve targets (and avail schemes) - that's the insight from our conversations with paint dealers in Mumbai. They told us, (1) Project business is severely impacted as construction workers, painters stay in distant suburbs and due to closure of public transport, they are not yet able to commute to Mumbai city, (2) waterproofing has performed well, however, on a smaller base, (3) All paint depots and dealers are operational now but with off-take level of 50-60% in July-Aug'20, and (4) There were no new launches and/or pricing actions in Jul-Aug'20.

Top picks are Akzo Nobel (only paint stock in our coverage rated BUY) - preferred turnaround pick for 2020 and beyond, Asian Paints (ADD). We recommend investors to wait for better entry points in our coverage of other paint stocks - Berger Paints and Kansai Nerolac are rated HOLD.

- ▶ **Paint market in Mumbai:** The Mumbai paint market is ~4% of annual revenues of Asian Paints as well as paint industry. The key market remained impacted in July-Aug'20. While all depots and almost all dealers are operational now, the off-take is still 50-60% of pre-Covid sales.
- ▶ **Change in trade schemes:** Asian Paints was offering trade scheme of 5-6% in May-June'20. However, it has now reduced trade schemes to 3-5% of sales. While the schemes up to Aug'20 were based on actual purchases by dealers, the scheme has changed from Sept'20 onwards. Now the dealers will be eligible for the scheme benefits if they achieve certain targets. In order to achieve the targets (and avail benefits), the dealers are likely to sell products of Asian Paints more. While Asian Paints may gain market share, volumes of other paint companies may get impacted.
- ▶ **Impact on projects business:** There is negligible demand from projects segment as of now. Construction labor, mason, plumbers and painters generally stay in distant suburbs (Ambarnath, Badlapur, Vasai, Virar etc). Due to lack of public transport, they are unable to travel to Mumbai city.
- ▶ **The association of paint dealers in Mumbai** is in discussion with Paint companies regarding issues like excess inventory (with some dealers), additional trade support, schemes etc. Dealers are hopeful of some solutions in coming months.
- ▶ **Waterproofing performing well:** Among all sub-segments of paints, the waterproofing is doing relatively well. However, it had very low base.
- ▶ **No new launches / pricing actions:** Paint companies have not yet increased / reduced prices of their products. There were no new launches in July-Aug'20.
- ▶ Dealers are hopeful that there will be demand recovery by Diwali i.e. mid-November.

We do channel checks. We do network checks. However, 20 years of experience has taught this analyst that on-the-ground checks have utility, if and only if, we don't extrapolate it as a national trend (as diversity is high in India). Worm's world view is our periodic product on network checks.

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**Table 1: Paint sector valuation summary**

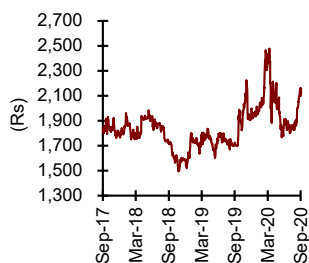
Company	CMP (Rs)	TP (Rs)	Upside (%)	Rating	PE (x)		EV/EBITDA (x)		ADTV (US\$ mn)	Market Cap	
					FY21E	FY22E	FY21E	FY22E		(Rs bn)	(US\$ bn)
Akzo Nobel	2,102	2,500	19	BUY	45	36	30	23	0.5	96	1.3
Asian Paints	1,956	2,200	12	ADD	70	55	44	36	60.2	1,919	25.6
Berger Paints	552	540	(2)	HOLD	93	76	56	47	12.1	551	7.4
Kansai Nerolac	486	460	(5)	HOLD	56	43	34	27	1.8	253	3.4

Company	EV/ sales (x)		P/B (x)		P/CEPS (x)		RoE (%)		RoCE (%)		CAGR (FY20-22E) (%)		
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	Revenues	EBITDA	PAT
Akzo Nobel	4.0	3.3	7	6	34	27	16	18	16	18	1	1	5
Asian Paints	9.2	7.4	17	14	54	44	25	28	22	25	12	12	12
Berger Paints	9.4	8.0	18	16	69	58	20	22	17	19	4	4	4
Kansai Nerolac	5.6	4.5	6	6	42	33	12	14	11	14	5	10	9

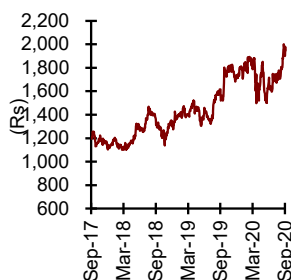
Source: Company data, I-Sec research

**Price charts**

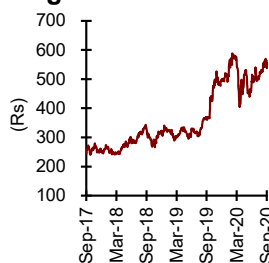
**Akzo Nobel**



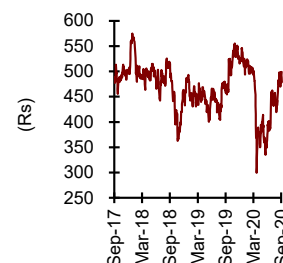
**Asian Paints**



**Berger Paints**



**Kansai Nerolac**



Source: Bloomberg

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