Choice
Nurturing Financial Excellence

Gujarat Fluorochemicals

BUY

'Positive business outlook'

May 19, 2021

Gujarat Fluorochemicals Limited (GFCL), earlier known as Inox Fluorochemicals Ltd, is the largest integrated producer of PTFE (poly tetra fluoro ethylene) resin in India & fourth largest in the world. GFCL has two manufacturing plants in India located in Gujarat Ranjitnagar (set up in 1989) and Dahej (set up in 2007). GFCL's core chemical business is fluoropolymer which accounts ~11% of world's total capacity. The company has become one of the most efficient Fluoropolymer producer in the globally efficiently utilized application in 20 industries such as automotive, aerospace, electronics among others.

GFCL also holds a leading position in manufacturing Hydrochlorofluorocarbon (HCFC) which is used in refrigeration and air conditioning. The company drives business across various chemical products namely Caustic Soda, Chloromethanes, Poly Tetrafluoroethylene, Refrigerant gases, New Fluoropolymers among others. GFCL generates around 35% of revenue from Poly Tetrafluoroethylene, ~15% each from Caustic Soda & Chloromethanes and ~18% from refrigerant gases. Thereby these four chemical products accounts for ~85% of the GFCL's operating revenue.

Investment Rationale:

- ✓ *Anti-dumping duty on fluorochemicals to boost business*
- ✓ *Cold storage to be a demand driver for refrigerant gases*
- ✓ *Improving profitability and margin*
- ✓ *Positive industry outlook and govt initiatives to provide boost to business*

View & Valuation

GFCL reported TTM sales (as of Q3FY21) of Rs2,443 cr as compared to Rs,2606 cr in FY20 which seems comforting given the pandemic hit first Q1FY21. EBIDTA margin improved to 21% in TTM period compared to 17% in FY20. In Q3FY21, GFCL reported 11% YoY sales growth to Rs634 cr, EBIDTA margin at 25% (2% YoY improvement) and PBT of Rs107 cr. Meanwhile the company reported loss of Rs480 cr due to charging of a non-recurring item of Rs539 cr to P&L during the quarter (due to settlement of disputed tax amount for the assessment fiscals FY08 to FY14.

Owing to its fully integrated manufacturing operations, company is a most competitive producer of fluorochemicals reflecting from its EBIDTA trend of above 20%. Company is a category leader in most of the segments that it operates in. GFCL strategized to focus on higher value added products in each of its segments with a focus to reduce competitions concerns from China. Moreover, entry barriers for a new competition also remains high due to complexity of business, extremely stringent and time consuming customer qualification and approval process. Some of the positive development for the business are improving capacity utilisation in PTFE, significant cost reduction in manufacturing process, likely strong growth in high margin products, high operating leverage and lower debt level with D/E at 0.35x.

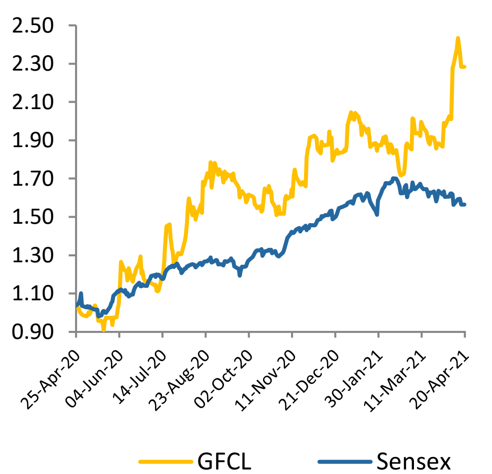
We expect GFCL to report a strong performance and sales to grow at a CAGR of 13% over FY20 to FY23E and margin to improve with better realisations and higher capacity utilization. At CMP of Rs816, GFCL's stock is trading at TTM P/E of 34.9x (adjusting with non-recurring tax payment). We assign 'Buy' rating to stock with target price of Rs940 valuing business at P/Ex of 26xFY23E.

Rating Matrix	
CMP	Rs816
Rating	Buy
Target price	Rs940
Holding period	12 Months
Upside (%)	15.2%
52 Week H/L	Rs870/280
Mar Cap	Rs8,966 cr
Face value	Rs1
Sector	Chemicals

Shareholding Pattern

Particulars	Jun'20	Sep'20	Dec'20	Mar'21
Promoters	68.4%	68.4%	68.4%	68.4%
FPIs	4.0%	2.3%	2.4%	2.3%
DIIs	7.0%	6.7%	5.8%	5.7%
Non. Inst.	20.6%	22.6%	23.4%	23.6%

Relative Capital Market Strength



Key Financials (Rs cr)

Particulars	FY20	FY21E	FY22E	FY23E
Net Sales	2,606	2,539	3,134	3,797
EBITDA	439	640	764	1017
EBITDA Mar. (%)	*16.8%*	*25.2%*	*24.4%*	*26.8%*
Adjusted PAT	196	-257	310	402
NPM (%)	*7.5%*	*-10.1%*	*9.9%*	*10.6%*
EPS (Rs)	17.8	-23.4	28.2	36.6
RoE (%)	5.3%	-7.4%	8.3%	9.8%
P/E (x)	45.6	-34.8	28.9	22.2
P/BV (x)	2.4	2.6	2.4	2.2
P/S (x)	3.4	3.5	2.9	2.4
EV/EBITDA	23.8	16.0	13.2	9.8

Investment Rationale:

Anti-dumping duty on fluorochemicals to boost business

The imposition of heavy anti-dumping duties by countries such as India and the US on China is expected to benefit GFCL to expand its chemical business products reach in domestic and overseas market. With its dominant position in fluorochemical business, the company is expected to remain major beneficiary of the move. As per the mgmt, domestic demand of PTFE came back to over 80% and overseas demand to be about 75% of pre-Covid level. Though second Covid wave to derail domestic recovery in the near term, the impact is likely to offset by buoyant demand in the global market. GFCL has developed a wide range of PTFE grades which qualified for extensive usages in various industries. Prices of PTFE are also expected to remain strong going forward which would boost largest segment's revenue.

Cold storage to be a demand driver for refrigerant gases

GFCL generates about 18% of total revenue (FY20) from refrigerant gas business. As India's faces challenge of food wastes due to lack of cold storage infrastructure, cold storage infrastructure in India is expected to rise in coming years with government supports. As per mgmt, production of refrigerants segment will continue to increase due to rising feedstock requirements, while prices of refrigerant are expected to remain stable. Furthermore, in near to mid term, refrigerant gases is expected to witness a sharp uptick following the demand for cold storage to store Covid-19 vaccine.

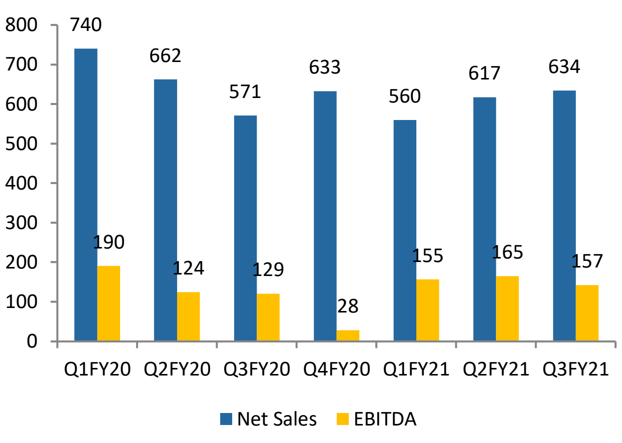
Improving profitability and margins

GFCL reported TTM sales (as of Q3FY21) of Rs2,443 cr as compared to Rs,2606 cr in FY20 which seems comforting given the pandemic hit first Q1FY21. While the EBIDTA margin improved to 21% in TTM period compared to 17% in FY20. In Q3FY21, GFCL reported 11% YoY sales growth to Rs634 cr, EBIDTA margin at 25% (2% YoY improvement) and PBT of Rs107 cr. However, GFCL reported loss of Rs480 cr due to charging of a non-recurring item of Rs539 cr to P&L during the quarter (due to settlement of disputed tax amount for the assessment fiscals FY08 to FY14.

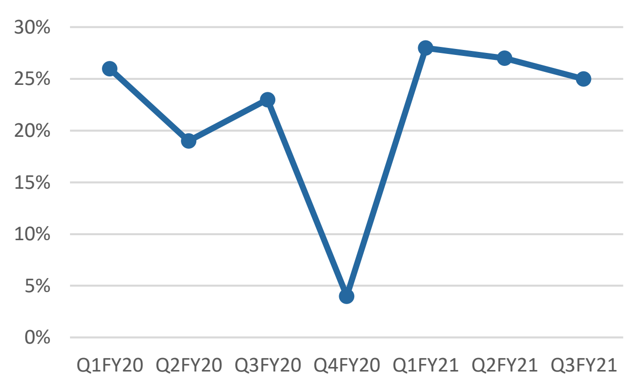
Positive Industry outlook and govt initiatives to provide boost to business

Government initiatives like Make-in-India and Atmanirbhar Bharat are expected to boost domestic industrial activities and boost exports in next five years. Chemical industry with potential of boost domesic exports is likely to be among the key beneficiaries industries. Outlook of chemical industry also turned positive as China, being the largest world chemical exporter, has started restricting its chemical production activities amid concern over environment safety. This has opened new exports opportunities for domestic chemical companies.

Operation performance improved



EBIDTA margin trend



Source: Choice Broking Research

Valuation and View:

Owing to its fully integrated manufacturing operations, company is a most competitive producer of fluorochemicals reflecting from its EBIDTA trend of above 20%. Company is a category leader in most of the segments that it operates in. GFCL strategized to focus on higher value added products in each of its segments with a focus to reduce competitions concerns from China. Moreover, entry barriers for a new competition also remains high due to complexity of business, extremely stringent and time consuming customer qualification and approval process. Some of the positive development for the business are improving capacity utilisation in PTFE, significant cost reduction in manufacturing process, likely strong growth in high margin products, high operating leverage and lower debt level with D/E at 0.35x.

We expect GFCL to report a strong performance and sales to grow at a CAGR of 13% over FY20 to FY23E and margin to improve with better realisations and higher capacity utilization. At CMP of Rs816, GFCL's stock is trading at TTM P/E of 34.9x (adjusting with non-recurring tax payment). We assign 'Buy' rating to stock with target price of Rs940 valuing business at P/Ex of 26xFY23E.

Peers Comparison

Companies (Rs cr)	CMP	ROE (%)	12MR (%)	M. Cap	EPS (Rs/sh)	BVPS (Rs/sh)	EBIDTA Margin (%)	NPM (%)
Bhansali Engineering Polymers	159	49.0%	312.0%	2,636.2	20.1	41.1	34.5%	25.9%
Gujarat Fluorochemicals	816	6.6%	128.7%	8,966.0	-27.6	351.6	20.1%	-12.4%
Linde India	1699	19.0%	246.4%	14,489.8	49.1	258.4	27.4%	27.3%
Navin Fluorine International	3188	15.8%	115.3%	15,779.6	52.1	330.1	26.2%	21.9%
Refex Industries	134	23.5%	159.9%	281.4	13.7	58.1	8.3%	4.8%
Average		***26.8%***	***192.5%***				***23.3%***	***13.5%***

Companies	P/E (x)	P/Bv (x)	P/Sales (x)	EV/EBIDTA (x)	D/E (x)	PAT	EBIDTA	Sales
Bhansali Engineering Polymers	7.9	3.9	2.0	5.6	0.0	334	446	1,291
Gujarat Fluorochemicals Ltd.	34.9	2.3	3.7	20.9	0.3	-303	491	2,444
Linde India	34.6	6.6	9.4	33.7	0.0	419	420	1,535
Navin Fluorine International	61.2	9.7	13.4	49.3	0.0	258	309	1,179
Refex Industries Ltd.	9.8	2.3	0.5	5.6	0.0	29	50	604
Average	**29.7**	**4.9**	**5.8**	**23.0**	**0.1**			

Companies	Out. Shares	Net Worth	EV	Debt	FV (Rs)	Cash	Equity Cap	Debt
Bhansali Engineering Polymers	17	681	2,483	0	1	153	16.6	**0**
Gujarat Fluorochemicals	11	3862	10,247	1,334	1	29	11.0	**1,334**
Linde India	9	2204	14,171	7	10	326	85.3	**7**
Navin Fluorine International	5	1634	15,238	3	2	544	9.9	**2**
Refex Industries Ltd.	2	122	280	2	10	3	21.0	**2**

Source: Choice Broking Research

Business Overview:
Two manufacturing facilities in India

1) Dahej (Bharuch District), Gujarat: GFCL produced chloralkali, chloromethane, PTFE and fluoropolymers.

2) Ranjitnagar (Ghogambha District), Gujarat: GFCL produced refrigerants gas and fluorospecialty intermediates

Other than 2 domestic plants, GFCL also has one international plant (Joint Venture) in Morocco (setup in 2011). In this facility, the company produces acid grade fluorspar mining and beneficiation used in manufacturing of Hydrofluoric Acid which is a key requirement for pharmaceuticals and chemical products. Morocco plant helps company allows it to connect with EU market.

Installed Capacity: - GFCL installed capacity of products such as: PTFE – 16,200 tpa, Caustic Soda – 1,34,750 pta, Chloromethane – 1,08,500, HCFC -65,000 pta. Around 50% business comes from India, ~20% from Eurore, ~12% from USA and balance from rest of world

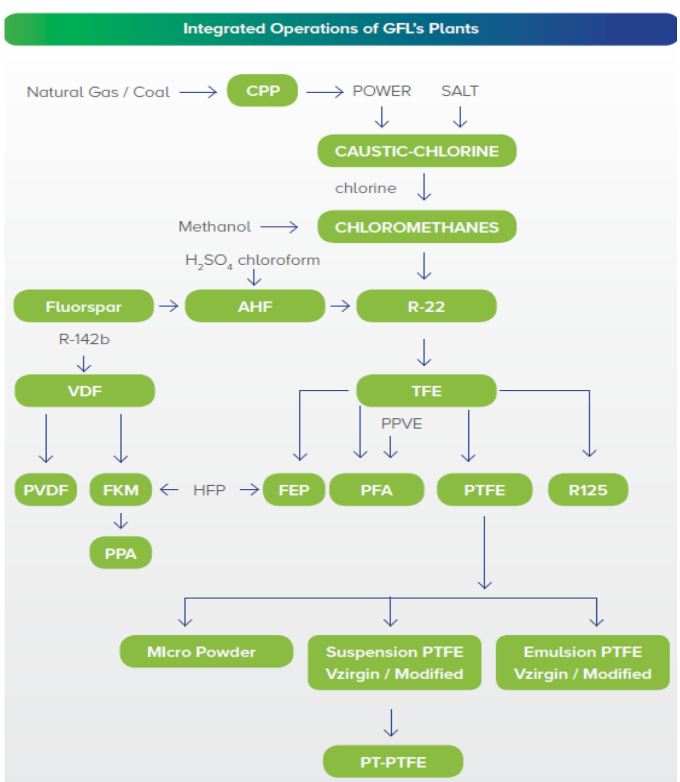
Products Profile

- **Refrigerants** GFCL is an established manufacturer and exporter of refrigerant gases R-12 & R-22. Its product are sold with a brand name Refron which are well accepted quality wise in international market. It supply refrigerant gases in bulk and disposable cylinders to its clients which are widely used in refrigerators, air-conditioners and as propellants for aerosols and as blowing agents for polyurethane foam production.

- **Chemicals:** Company focuses on innovation and sustainability to cater wide industries with its diversified chemical portfolio. Under chemical business segment, it comprises Caustic soda lye, methylene chloride, hydrogen gas, AHCL, HCL and H2SO4. Its chemical complex is situated at Dahej and has coal & gas based captive power plant with a capacity of ~90 MW.

- **Fluoropolymers:** With its two modern & backward-integrated PTFE manufacturing facilities in Dahej, it produces a wide range of suspension & emulsion fluoropolymers resins. Its fluoropolymers resin are sold in market under the brand name Inoflon that caters to requirements of applications that require to operate under high temperature and extensive chemical pressure, most commonly found in industries like automotive, aerospace, oil and gas, food and pharmaceutical.

- **Fluorospecialty Business:** Unique building blocks, capabilities and facilities produces fluorospecialty products and intermediates to cater industries like agrochemical, pharmaceutical, electronic and polymer industries. It also has a fluorospecialty analytical cell with advanced equipment.



Consolidated (Rs cr)

P&L	FY20	FY21E	FY22E	FY23E
Net Sales	2,606	2,539	3,134	3,797
EXPENDITURE :				
Increase/Decrease in Stock	-103	-50	-72	-76
Raw Material Consumed	864	853	1,014	1,166
Power & Fuel Cost	481	0	0	0
Employee Cost	205	495	621	734
Other Manufacturing Expenses	453	441	546	645
General and Administration Expenses	116	222	260	311
Selling and Distribution Expenses	3	-27	0	0
Miscellaneous Expenses	148	-34	0	0
Total Expenditure	2,167	1,899	2,369	2,780
EBITDA	**439**	**640**	**764**	**1,017**
Depreciation	192	207	244	292
EBIT	247	434	520	726
Other Income	216	142	197	179
Interest	105	121	136	165
Exceptional Income / Expenses	-26	0	0	0
Profit Before Tax	332	454	581	739
Tax	143	718	278	344
Profit After Tax	189	-264	303	395
Minority Interest	7	7	7	7
Consolidated Net Profit	**196**	**-257**	**310**	**402**

Balance Sheet	FY20	FY21E	FY22E	FY23E
Share Capital	11	11	11	11
Total Reserves	3,705	3,448	3,727	4,089
Shareholder's Funds	3,716	3,459	3,738	4,100
Minority Interest	-11	-11	-11	-11
Total Non-Current Liabilities	280	273	337	408
Trade Payables	367	358	441	535
Other Current Liabilities	400	390	481	583
Short Term Borrowings	1,042	1,015	1,253	1,518
Short Term Provisions	34	195	769	1,359
Total Current Liabilities	1,843	1,957	2,945	3,995
Total Liabilities	**5,828**	**5,679**	**7,009**	**8,492**
Net Block	2,404	2,342	2,891	3,502
Capital Work in Progress	318	310	383	464
Total Non-Current Assets	3,901	3,801	4,692	5,684
Currents Investments	67	66	81	98
Inventories	813	792	977	1,184
Sundry Debtors	565	550	679	823
Cash and Bank	17	16	20	24
Other Current Assets	65	63	78	94
Short Term Loans and Advances	401	391	482	584
Total Current Assets	1,927	1,878	2,317	2,808
Total Assets	**5,828**	**5,679**	**7,009**	**8,492**

Financial Ratios	FY20	FY21E	FY22E	FY23E
Profitability Ratios				
RoE (%)	5.3%	-7.4%	8.3%	9.8%
RoA (%)	3.4%	-4.5%	4.4%	4.7%
ROCE (%)	4.7%	8.8%	9.3%	11.5%
Operating Ratios				
Sales Gr. (%)		-2.6%	23.4%	21.2%
EBIDTA Gr. (%)		45.9%	19.4%	33.1%
PAT Gr. (%)		-231.1%	-220.7%	29.8%
EBIDTA Margin (%)	16.8%	25.2%	24.4%	26.8%
NPM (%)	7.5%	-10.1%	9.9%	10.6%
EPS (Rs)	17.8	-23.4	28.2	36.6
BVPS (Rs)	338.2	314.9	340.3	373.2
Valuation Ratios				
P/E (x)	45.7	-34.9	28.9	22.3
P/BV (x)	2.4	2.6	2.4	2.2
P/S (x)	3.4	3.5	2.9	2.4
EV/EBIDTA (x)	23.8	16.0	13.3	9.9

Source: Choice Broking Research

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Choice's Rating Rationale

The price target for a large cap stock represents the value the analyst expects the stock to reach over next 12 months. For a stock to be classified as Outperform (Buy), the expected return must exceed the local risk free return by at least 5% over the next 12 months. For a stock to be classified as Underperform (Reduce, Sell), the stock return must be below the local risk free return by at least 5% over the next 12 months. Stocks between these bands are classified as Neutral (Hold).

BUY	Absolute Return >15%
Hold	Absolute Return Between 0-15%
Reduce	Absolute Return 0 To Negative 10%
Sell	Absolute Return > Negative 10%

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