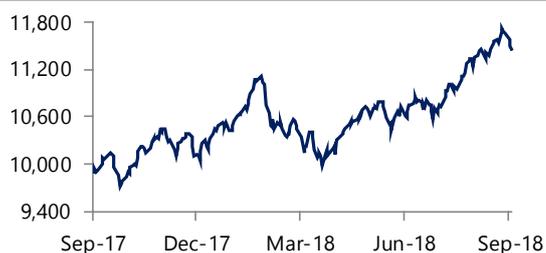


SEPTEMBER 6, 2018

	5-Sep	% Chg			
		1 Day	1 Mth	3 Mths	
Indian Indices					
SENSEX Index	38,018	(0.4)	1.2	8.9	
NIFTY Index	11,477	(0.4)	1.0	8.3	
NSEBANK Index	27,376	(0.2)	(1.2)	4.3	
NIFTY 500 Index	9,765	(0.4)	0.8	7.2	
CNXMcap Index	19,246	(0.4)	0.7	5.8	
BSESMCAP Index	16,728	(0.5)	(0.6)	3.1	
World Indices					
Dow Jones	25,975	0.1	1.9	3.3	
Nasdaq	7,995	(1.2)	1.7	4.0	
FTSE	7,383	(1.0)	(3.7)	(4.3)	
NIKKEI	22,581	(0.5)	0.1	(0.4)	
Hangseng	22,581	(0.5)	0.1	(0.4)	
Shanghai	27,244	(2.6)	(2.5)	(13.2)	
Value traded (Rs cr)		5-Sep	% Chg Day		
Cash BSE		3,527	(7.2)		
Cash NSE		37,076	3.6		
Derivatives		1,357,421	33.4		
Net inflows (Rs cr)		4-Sep	MTD	YTD	
FII		1,619	3,055	(2,384)	
Mutual Fund		285	285	76,902	
Nifty Gainers & Losers		Price	Chg	Vol	
5-Sep		(Rs)	(%)	(mn)	
Gainers					
Yes Bank Ltd		344	2.9	24.8	
Vedanta Ltd		229	2.1	10.4	
Hindalco Ind		240	2.1	11.4	
Losers					
Bharti Infra		271	(4.5)	2.1	
Hindustan Unilever		1,612	(2.4)	2.7	
Zee Entertainment		482	(2.2)	2.4	
Advances / Declines (BSE)					
5-Sep	A	B	T	Total	% total
Advances	168	309	62	539	100
Declines	261	724	89	1,074	199
Unchanged	3	19	15	37	7
Commodity		% Chg			
	5-Sep	1 Day	1 Mth	3 Mths	
Crude (US\$/BBL)	77.1	(0.2)	4.5	2.3	
Gold (US\$/OZ)	1,197	0.5	(0.6)	(7.5)	
Silver (US\$/OZ)	14.2	0.2	(7.0)	(14.7)	
Debt / forex market		5-Sep	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %		8.1	8.1	7.8	7.8
Re/US\$		71.8	71.6	68.9	67.2

Nifty



Source: Bloomberg

News Highlights

- ▶ Securities and Exchange Board of India (Sebi) said it will review the proposed new norms for foreign portfolio investors and take a holistic view after taking into account views of all stakeholders, including the government. (Mint)
- ▶ The centre is formulating a policy to substitute imported goods with domestic products, of which electric vehicles will form a major part, said Union minister for road transport, highways and shipping, Nitin Gadkari. (Mint)
- ▶ Qatar Airways has said that it would be interested in Air India only if it comes without the 'baggage', after the government decided to hold the national carrier's divestment plans following a failed attempt to attract bidders. (ET)
- ▶ **Bharat Electronics Ltd** said it has entered into a contract with Mazagon Dock Limited (MDL) and Garden Reach Shipbuilders and Engineers (GRSE) to supply LRSAM systems. A Rs 92 bn order for supply of seven long range surface-to-air missile (LRSAM) systems has pushed the order book of state-run Bharat Electronics Ltd beyond Rs 500 bn for the first time in a single financial year, the company. (ET)
- ▶ Larsen and Toubro Infotech said its promoter **Larsen and Toubro (L&T)** has offloaded 6.08 per cent stake in the company, paring the parent's shareholding to 75 per cent. (ET)
- ▶ The Rs160 bn buyback programme of **Tata Consultancy Services** will begin today and close on September 21. (BL)
- ▶ **Hindustan Petroleum Corporation Ltd's (HPCL)** long-delayed refinery and petrochemicals complex in Rajasthan is finally taking shape. HPCL will shortly raise Rs280 bn in debt from a consortium of banks, two officials at HPCL told. (Mint)
- ▶ **Apollo Tyres** said production operations at its plants in Kerala have reached near normalcy post floods. (ET)
- ▶ Centrum Financial Services Ltd, the NBFC arm of the **Centrum** Group, said that it had acquired the supply chain business of L&T Finance. (Mint)
- ▶ **Union Bank of India** hopes to recover Rs20 bn from the resolution of three stressed thermal power units as there has been interest from other operators in these projects. (Mint)
- ▶ **Tata Motors'** August JLR UK sales was up 66 percent at 3,444 units against 2,077 units in the same month last year. Tata Motors JLR sold 9,648 units, growth of 2 percent, in the US market. (Moneycontrol)

What's Inside

- ▶ **Company Update:** Akzo Nobel India Ltd

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, IE = Indian Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange, MC = Moneycontrol

Management Meet Update

AKZO NOBEL INDIA LTD (AKZO)

Stock Details

Market cap (Rs mn)	:	80412
52-wk Hi/Lo (Rs)	:	1999 / 1688
Face Value (Rs)	:	10
3M Avg. daily vol (Nos)	:	11,731
Shares o/s (mn)	:	46

Source: Bloomberg

Financial Summary

Y/E Mar (Rs mn)	FY18	FY19E	FY20E
Revenue	28,318	32,865	36,181
Growth (%)	0.2	16.1	10.1
EBITDA	2,992	3,814	4,450
EBITDA margin (%)	10.6	11.6	12.3
PAT	2,037	24,732	28,099
EPS	44.7	55.8	64.7
EPS Growth (%)	0.5	22.0	13.6
BV (Rs/share)	245.4	289.8	318.1
Dividend/share (Rs)	22.5	25.0	32.4
ROE (%)	19.0	20.9	21.3
ROCE (%)	25.1	27.2	28.7
P/E (x)	38.5	30.8	26.6
EV/EBITDA (x)	22.0	17.6	15.3
P/BV (x)	7.0	5.9	5.4

Source: Company, Kotak Securities - PCG

Shareholding Pattern (%)

(%)	Jun-18	Mar-18	Dec-17
Promoters	73.0	73.0	72.3
FII	1.5	1.7	1.9
DII	9.0	9.0	8.5
Others	16.5	16.3	17.3

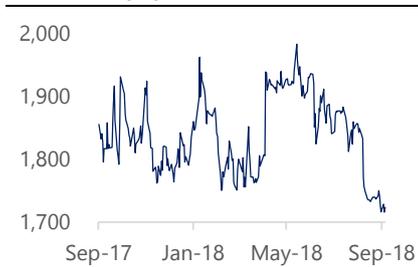
Source: Company

Price Performance (%)

(%)	1M	3M	6M
Akzo Nobel	(6.8)	(10.3)	(3.2)
Nifty	1.0	8.3	10.8

Source: Bloomberg

Price chart (Rs)



Source: Bloomberg

Amit Agarwal

agarwal.amit@kotak.com
+91 22 6218 6439

PRICE Rs.1720

TARGET Rs.2200

BUY

Stable performance in both the key segments of decorative and industrial paints over many quarters, renewed aggression under a new management, favourable macro environment, reduction in GST and raw material price inflation would be the highlights of the performance for Akzo in near term. For Akzo, we estimate 11% volume CAGR over FY18 – FY20E with stable margins and ROE of ~23% and ROCE of ~21.9% for FY20E. Maintain BUY with an unchanged TP of Rs 2200 at 34x FY20E earnings (at 25% discount to PE multiple of peers).

Decorative segment

In the decorative segment, Akzo has a presence in premium as well as mass market and economy segments, with strong positioning in the premium segment through its well established brand "DULUX". Akzo manufactures the Dulux brand of paints for interior and exterior decoration and protection as well as products for surface preparation and wood care. The focus of the company is on quality, aesthetics and high performance in terms of longevity, washability and stain resistance, anti-color fading, water proofing, ease of application, faster drying times, low VOC and odour, and so on. The paints are also free from any added lead, mercury or chromium compounds, underlining the importance that Akzo gives to caring for the environment.

Product portfolio of Akzo in Decorative segment

Product name	Market	Usage	Striking features
Dulux Velvet Touch 'Pearl Glo'	Premium	Interior wall finish	Washability, stain resistance and anti-fungal properties
Dulux Velvet Touch 'Trends'	Premium	Interior wall finish	Designer
Dulux WeatherShield	Mid	Exterior	Temperature resistant
Dulux WeatherShield Max	Mid	Exterior	Long lasting, anti-fungal
Dulux WeatherShield Ultra Clean	Premium	Exterior	High performance, durable
Dulux WeatherShield Clear	Mid	Exterior	Anti-fungal
Dulux WeatherShield Tex	Mid	Exterior	Tough, durable and water repellent
Dulux TileShield	Mid	Exterior	Long-lasting protection and an aesthetic appearance
Dulux Promise	Low	Exterior	Economical, superior technology and environment-friendly
Dulux Gloss	Premium	Wood and metal finish	Superior and tough finish

Source: Company

In FY18, Akzo launched a series of innovative and environment friendly new products, which as per management has received good response from the market. Some of them are:

- Dulux Aquatech – water proofing range,
- WeatherShield Flash – two coat system, revolutionary technology for exterior walls,
- Supercover Sheen – entry level sheen product in premium emulsion.

The main drivers for the growth of this business in a country like India includes,

- 1) Regular launch of new products
- 2) Aggressive marketing
- 3) Push at the dealer level
- 4) Shortening of the repainting cycle
- 5) Increased demand from smaller towns.
- 6) Macro developments like nuclear families, availability of easy finance for housing and government's thrust on affordable housing

From the above mentioned triggers, points 4 to 6 is same for all the companies. While for points 1 to 3, Akzo lags behind larger peers.

Brief Comparison of paint companies

Parameter	Akzo	APL	KNPL	Berger
No of Dealers	9,000	42,000	20,000	20,000
No of Tinting Machines	7,000	30,500	15,000	14,000
Focus Area	High to Mid	All	High to Mid	Mid
Focus segment	Decorative	Decorative	Industrial	Decorative
Key Markets in India	North	Pan India	North West	North East
Decorative Segment market share (%)	8	45	7	12.5
Industrial Segment market share (%)	3	15	21	9
Promotional expenditure in decorative (%)	5	7	9	7
Operating Margins (%)	12	19	18	16

Source: Companies

Industrial Paints

We estimate that the industrial paints segment contributes approximately 10% of the overall revenues of the company. Management expects this segment to do well in FY19, as it is a pre-election year. Industrial paints segment is a B2B business and margins tend to be lower in this segment due to corporate nature of the client and scale of the business. Also in this business, a single customer is usually catered by more than one paint company. Currently, Akzo has a market share of 3% in the segment and management has internally set a target ROI of 25% from this business which would augment the overall profits of the company.

Presence of Akzo in Industrial paints

Segment	Usage	Outlook
Marine coating	Ship Construction	Neutral
Powder coating	Automobiles, white goods, General Industrial	Positive
Metal coating	Building and construction	Positive
Vehicle refinishes	Vehicle repairs	Positive

Source: Company

Company's Business Strategy

Our interaction with the management of Akzo indicate that the focus of the company would be to build a sustainable business for long-term value creation. This includes focus on margins and earnings (and not sales). Hence, the company is not focusing on aggressively improving its geographical reach beyond its current markets of North and East India, but focusing more on improving the product mix, bring down fixed cost and improving efficiency for superior financial performance. To pursue its strategy, Akzo also divested its specialty chemicals business as a going concern to an affiliate of the Akzo Nobel Group for Rs 3.1 bn. The intention of the company here was to focus on core decorative and industrial

painting business post demerger in line with business of any conventional paint company. We expect this strategy to be helpful for the Indian business. It is commendable that the performance of the company in Q1FY19 was largely unaffected post the demerger (no significant decline in Sales and PAT).

Details of the Divestment of the specialty business

Parameter	Value
FY18 sales	Rs 2387 mn
FY18 EBIT	Rs 196 mn
Net consideration to Akzo	Rs 3.1 bn
Buy back amount	Rs 2.35 bn
Buy back %	2.4

Source: Company

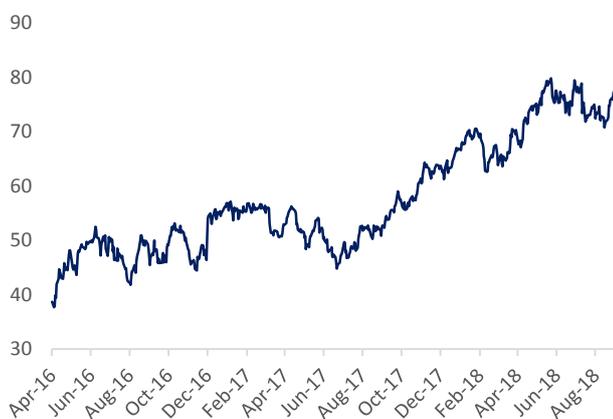
Buy back completed – equity capital reduced by 2.4%

The company had utilized the proceeds of the sales of the specialty chemical business to buy-back shares worth Rs 2.35 bn at Rs 2100 per share which translates into 1.12 mn shares or 2.4 % of the total equity of the company. The buy-back completed on July26th. We believe the buyback is one of the ways to reward the non-promoter’s shareholders of the company rather than giving a special dividend which would have attracted Dividend Distribution Tax. We see this buyback as a positive signal for the stock. The buy-back has reduced the equity capital of the company from Rs 467 mn (46.7mn shares) to Rs 455.8 mn (45.6 mn shares).

Raw Material cost outlook is not healthy

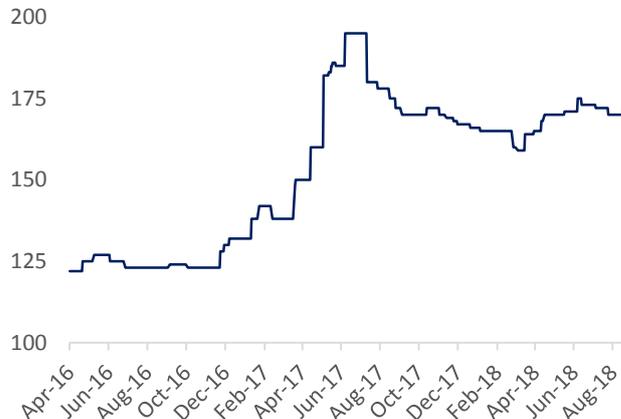
Paint Industry uses two key raw material including crude derivatives and Titanium Dioxide. The Paint Industry is experiencing increase in prices of raw material since the last 4 quarters. Almost ~60% of the raw material are crude derivatives and with crude at \$78/barrel (+50% YoY), prices of crude derivatives have also increased. Even prices of pigments like Titanium Dioxide, Iron oxide and Zinc oxide have increased. Even INR volatility has contributed to cost inflation for the company. To counter this, the management of paint companies including Akzo have resorted to price increase and cost optimization. We expect Akzo to completely pass on cost inflation to consumers by end of FY19 and report strong operational performance.

Prices of crude in US\$



Source: Bloomberg

Prices of Titanium dioxide (\$/MT)



Source: Bloomberg

Latest development – reduction in GST a big positive for the company

Paint industry was paying excise of 12.5% and 15% VAT under the old regime. So introduction of GST rate of 28% in July 2017 did not change the price at the consumer end with some adjustment happening only at the dealer end.

Post the current reduction of GST rate from 28% to 18% (from 27th July, 2018), we expect paint companies (they had shown intent earlier also) to reduce the prices and pass on the benefit partially to consumers which is estimated to boost the volumes for paint industry. Partially the benefit of lower GST may be retained (in the long-run) by the paint companies as a cushion against rising raw material prices. Both the reactive steps by the industry would aid the margins and bottom line of paint companies going forward. It is important to note that Akzo has already reduced product prices proportionate to decrease in GST rates.

Valuation and Outlook

We estimate that branded paint demand will remain robust in a country like India where per capita consumption is very low and 30% paint market is still unorganised. Management of Akzo also indicated that the volume trends remain strong for the company and expect the trend to continue in medium term. For Akzo, we estimate 11% volume CAGR over FY18 – FY20E with stable margins and ROE of ~23% and ROCE of ~21.9% for FY20E. Maintain BUY with an unchanged TP of Rs 2200 at 34x FY20E earnings (at 25% discount to PE multiple of peers).

Company background

Akzo Nobel NV, the world's largest paints company, operates in India through its subsidiary Akzo Nobel India (AKZO) which it acquired as a part of the global acquisition of Imperial Chemicals Industries (ICI) Plc. in FY08 for USD16bn. Its brand portfolio includes well-known brands such as Dulux, Sikkens, Glidden and International. The company has its headquarter in Amsterdam and operates in more than 80 countries. Akzo in India enjoys ~8% market share in decorative paints in India serviced through its network of 9000 plus dealers, 90 depots and six manufacturing facilities.

Financials: Consolidated

Profit and Loss Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Revenues	28,249	28,318	32,865	36,181
% change YoY	7.0	0.2	16.1	10.1
RawMaterial	15,826	16,182	18,596	20,270
Employee cost	2,625	2,490	2,960	3,267
Other expenses	6,310	6,654	7,494	8,194
Total Operating expd	24,761	25,326	29,050	31,731
EBITDA	3,488	2,992	3,814	4,450
Depreciation	565	595	657	708
EBIT	2,923	2,397	3,157	3,742
Other income	493	460	500	500
Interest expense	32	37	24	28
Profit before tax	3,384	2,820	3,633	4,213
Tax	953	783	1,090	1,264
ETR (%)	28.2	27.8	30.0	30.0
Profit after tax	2,431	2,037	2,543	2,949
JV & Associates	0	0	0	0
Net income	2,431	2,037	2,543	2,949
% change YoY	7.0	0.5	22.0	13.6
Shares outstanding (m)	46	46	46	46
EPS	53.3	44.7	55.8	64.7

Source: Company, Kotak Securities – Private Client Research

Cash flow Statement (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
PAT	2,431	2,037	2,543	2,949
Depreciation +DTL	278	673	766	835
Change in working capital	(963)	132	119	(108)
Cash flow from operations	1,746	2,842	3,428	3,676
Capex	(670)	(595)	(589)	(634)
Investments	2,692	(261)	(200)	(300)
Cash flow from investments	2,022	(856)	(789)	(934)
Equity issuance	-	-	(2,350)	-
Debt raised	11	51	46	46
Dividend Paid	(3,903)	(1,242)	(1,379)	(1,784)
Miscellaneous items	39	-	3,100	-
Cash flow from financing	(3,853)	(1,191)	(583)	(1,738)
Net cash flow	(85)	795	2,057	1,003
Opening cash	1,318	1,233	2,028	4,085
Closing cash	1,233	2,028	4,085	5,088

Source: Company, Kotak Securities – Private Client Research

Balance sheet (Rs mn)

(Year-end Mar)	FY17	FY18	FY19E	FY20E
Cash	1,233	2,028	4,085	5,088
Debtors	4,121	3,954	4,692	5,109
Inventory	4,054	4,018	4,624	5,139
Loans & advances	13	20	20	20
Other current assets	681	637	766	829
Total current assets	8,869	8,630	10,102	11,096
LT investments	3,439	3,700	3,900	4,200
Net fixed assets	5,423	5,423	5,354	5,280
Total assets	18,965	19,781	23,443	25,666
Creditors	6,232	5,891	7,140	7,790
Provisions	839	939	1,017	1,131
Other current liabilities	1,442	1,575	1,839	1,961
Total current liabilities	8,513	8,405	9,996	10,882
LT debt	140	191	237	283
Minority Interest	0	0	0	0
Equity Capital	456	456	456	456
Reserves	9,856	10,729	12,753	14,044
Networth	10,312	11,185	13,208	14,500
Total liabilities	18,965	19,781	23,443	25,666

Source: Company, Kotak Securities – Private Client Research

Ratio Analysis

(Year-end Mar)	FY17	FY18	FY19E	FY20E
EBITDA margin (%)	12.3	10.6	11.6	12.3
EBIT margin (%)	10.3	8.5	9.6	10.3
Net profit margin (%)	8.6	7.2	7.7	8.2
ROE (%)	21.8	19.0	20.9	21.3
ROCE (%)	32.7	25.1	27.2	28.7
DPS	71.0	22.5	25.0	32.4
CEPS	65.7	57.7	70.2	80.2
Book Value (Rs/share)	226.2	245.4	289.8	318.1
Working capital turnover (days)	(1.6)	3.7	1.8	1.6
Debt Equity (x)	0.0	0.4	0.2	0.0
PER (x)	32.2	38.5	30.8	26.6
P/C (x)	26.2	29.8	24.5	21.4
Dividend yield (%)	4.1	1.3	1.5	1.9
P/B (x)	7.6	7.0	5.9	5.4
EV/Sales (x)	2.7	2.7	2.3	2.1
EV/ EBITDA (x)	19.0	22.0	17.6	15.3

Source: Company, Kotak Securities – Private Client Research

RATING SCALE

Definitions of ratings

- BUY** – We expect the stock to deliver more than 12% returns over the next 12 months
- ACCUMULATE** – We expect the stock to deliver 5% - 12% returns over the next 12 months
- REDUCE** – We expect the stock to deliver 0% - 5% returns over the next 12 months
- SELL** – We expect the stock to deliver negative returns over the next 12 months
- NR** – **Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
- SUBSCRIBE** – We advise investor to subscribe to the IPO.
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- NA** – **Not Available or Not Applicable.** The information is not available for display or is not applicable
- NM** – **Not Meaningful.** The information is not meaningful and is therefore excluded.
- NOTE** – Our target prices are with a 12-month perspective. Returns stated in the rating scale are our internal benchmark.

FUNDAMENTAL RESEARCH TEAM

<p>Rusmik Oza Head of Research rusmik.ozakotak.com +91 22 6218 6441</p>	<p>Arun Agarwal Auto & Auto Ancillary arun.agarwal@kotak.com +91 22 6218 6443</p>	<p>Amit Agarwal Transportation, Paints, FMCG agarwal.amit@kotak.com +91 22 6218 6439</p>	<p>Nipun Gupta Information Tech, Midcap nipun.gupta@kotak.com +91 22 6218 6433</p>	<p>Krishna Nain Special Situations krishna.nain@kotak.com +91 22 6218 7907</p>
<p>Sanjeev Zarbade Cap. Goods & Cons. Durables sanjeev.zarbade@kotak.com +91 22 6218 6424</p>	<p>Ruchir Khare Cap. Goods & Cons. Durables ruchir.khare@kotak.com +91 22 6218 6431</p>	<p>Jatin Damania Metals & Mining, Midcap jatin.damania@kotak.com +91 22 6218 6440</p>	<p>Cyndrella Carvalho Pharmaceuticals cyndrella.carvalho@kotak.com +91 22 6218 6426</p>	<p>K. Kathirvelu Support Service k.kathirvelu@kotak.com +91 22 6218 6427</p>
<p>Teena Virmani Construction, Cement, Building Mat teena.virmani@kotak.com +91 22 6218 6432</p>	<p>Sumit Pokharna Oil and Gas, Information Tech sumit.pokharna@kotak.com +91 22 6218 6438</p>	<p>Pankaj Kumar Midcap pankajr.kumar@kotak.com +91 22 6218 6434</p>	<p>Jayesh Kumar Economist kumar.jayesh@kotak.com +91 22 6218 5373</p>	

TECHNICAL RESEARCH TEAM

<p>Shrikant Chouhan shrikant.chouhan@kotak.com +91 22 6218 5408</p>	<p>Amol Athawale amol.athawale@kotak.com +91 20 6620 3350</p>
--	--

DERIVATIVES RESEARCH TEAM

<p>Sahaj Agrawal sahaj.agrawal@kotak.com +91 79 6607 2231</p>	<p>Malay Gandhi malay.gandhi@kotak.com +91 22 6218 6420</p>	<p>Prashanth Lalu prashanth.lalu@kotak.com +91 22 6218 5497</p>	<p>Prasenjit Biswas, CMT, CFTe prasenjtit.biswas@kotak.com +91 33 6625 9810</p>
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Kotak Securities Limited. Registered Office: 27 BKC, C 27, G Block, Bandra Kurla Complex, Bandra (E), Mumbai 400051. CIN: U99999MH1994PLC134051, Telephone No.: +22 43360000, Fax No.: +22 67132430. Website: www.kotak.com/www.kotaksecurities.com. Correspondence Address: Infinity IT Park, Bldg. No 21, Opp. Film City Road, A K Vaidya Marg, Malad (East), Mumbai 400097. Telephone No: 42856825. SEBI Registration No: NSE INB/INF/INE 230808130, BSE INB 010808153/INF 011133230, MSE INE 260808130/INB 260808135/INF 260808135, AMFI ARN 0164, PMS INP000000258 and Research Analyst INH000000586. NSDL/CDSL: IN-DP-NSDL-23-97. Our research should not be considered as an advertisement or advice, professional or otherwise. The investor is requested to take into consideration all the risk factors including their financial condition, suitability to risk return profile and the like and take professional advice before investing. Investments in securities market are subject to market risks, read all the related documents carefully before investing. Derivatives are a sophisticated investment device. The investor is requested to take into consideration all the risk factors before actually trading in derivative contracts. Compliance Officer Details: Mr. Manoj Agarwal. Call: 022 - 4285 8484, or Email: ks.compliance@kotak.com.

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