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SRF RATING: **BUY**

Growth prospects in chemicals

The company can sustain a high capex environment over the next five years

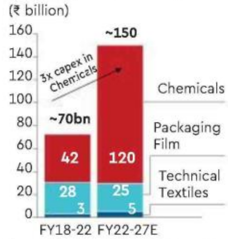
WE INTERACTED WITH Ashish Bharat Ram, along with the various heads of segments. SRF is optimistic about solid growth opportunities in the chemicals business driven by a fast changing geopolitical environment. This will usher in aggressive capex plans in chemicals (~₹120 bn over the next five years). SRF is also uniquely positioned to divert its solid cash flows from the commodity business to chemicals, which enjoys higher margins and return ratios. We are aligned with management's view of a favourable industry scenario and are gung-ho about its capex plans, which can treble its chemical segment Ebitda over the next five years. Retain 'BUY' with a SoTP-based TP of ₹3,128.

Management meeting and annual report: Key takeaways

- SRF is confident about strong growth opportunities in the chemical space in the medium and long-term. It will aggressively invest ₹120-130 bn over the next five years in the space while keeping the hurdle rate at north of 20% RoCE.
- Agrochemicals to grow at 20%-plus p.a. over the next 2-3 years; accelerated focus in pharma to support growth in the medium-term. Electronics and battery chemicals to unleash future growth potential in the long-term.
- Foray into PTFE (polytetrafluoroethylene) will unleash growth in fluoropolymers where SRF will leverage its fluorination capability. Its undisputed leadership in refrigerant gases and strong demand environment in HFCs will keep the revenue and margins strong.
- SRF has generated solid cash flows in the last five years – partially diverted from a commodity nature (packaging film and technical textile) to chemicals business, which enjoys higher margins, RoCE and commands premium valuations.
- Witnessed solid FY22 Ebitda growth (48% y-o-y) as favourable pricing environment in refrigerant gases and technical textiles boosted margins. This has led to 600bp RoCE improvement to 24.7% and strong free cash flow generation.

Sharp jump in capex

(₹ billion)



Source: Company, Edelweiss Research

Outlook and valuation: Multiple growth levers; retain 'BUY'

We believe, SRF's chemical business has catapulted strong growth opportunity and can sustain a high capex environment over the next five years while enjoying higher margins and return ratios. We believe, long-term growth opportunity will remain intact amid muted PAT growth expectations in FY24E (2% y-o-y) – margin pressure in packaging film, technical textile and refrigerant gases over next 4-6 quarters on the back of peak margins enjoyed by these businesses over the last 4-6 quarters. Our SoTP-based target price of ₹3,128 values SRF's chemicals business at 32x EV/Ebitda and technical textile and packaging film at 12x each, based on Q3FY24E estimates. We retain 'BUY/SO'. Contraction in margins in packaging film and refrigerant gases pose near-term concerns. Failure in pick up in its fluoropolymers, pharma specialty chemicals may risk our estimates.

EDELWEISS