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SRF's chemicals biz may drive growth but margins are sore point

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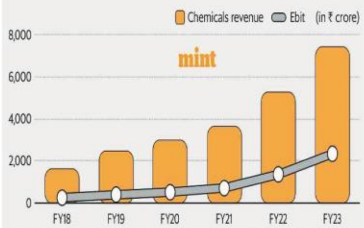
1 Shares of SRF Ltd have been flat in the past one year and are now nearly 20% lower than its 52-week highs of ₹2,865 apiece seen in September. While the company's chemicals business is on a reasonably good footing, the problem is that SRF's other two segments, technical textiles and packaging films businesses have not been firing enough.

Weaker demand and higher input costs have weighed on these businesses in FY23. These segments contributed 25.6% of SRF's FY23 consolidated earnings before interest and tax (Ebit). Year-on-year, both segments saw a drop of about 900 basis points each in Ebit margin in FY23.

Outlook largely remains dull. "The packaging film segment is expected to witness moderate growth going ahead as margin pressure is likely to continue for the near term. Increasing share of value-added products and operational efficiency will aid profitability," said Motilal Oswal Financial Services analysts in a 27 June report. "The technical textile business is expected to recover on the back of improving NTCF demand and capacity addition in belting fabrics segment. Margins are likely to stay under pressure due to cheap imports from China." Nylon Tyre Cord Fabric is NTCF.

Key catalyst

SRF's chemicals business is expected to continue to drive growth in FY24.



Note: Ebit is earnings before interest and tax Source: Company, Motilal Oswal Financial Services

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Further, SRF's chemicals business is expected to continue to drive growth in FY24 as well, though margin trajectory could be a dampener. Chemicals business growth would be aided by continuous capital expenditure (capex) and new product launches. For FY24, the company has planned capex of ₹2,500 crore, out of which the lion's share will be for chemicals. It plans to commission 10 plants in FY24 in segment, launch 7-8 active ingredients in agrochemical and increase focus on pharma segments. Management expects chemicals revenue growth of over 20% in FY24. In FY23, this segment's revenue grew 41% year-on-year.

However, in the June quarter (Q1FY24), performance of refrigerant gas business could be soft owing to erratic weather in domestic market. Chemicals business comprises specialty chemicals and fluorochemicals (including refrigerant gas).

"The refrigerant gas prices have seen some correction in the past few months," Rohan Gupta, director, Nuvama Institutional Equities, said. "With weak demand currently in exports and domestic, prices may remain under pressure with further price correction. It remains to be seen if demand recovers after Q2FY24," he added. All said, lingering margin pressures are likely to keep sentiments for the stock subdued in near term even after last one year's returns have been muted.