



PAINT SECTOR OVERVIEW

Introduction to Paint Industry

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Team Ficus!

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Paints & Coatings:

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To meet this market demand, BASF develops and delivers innovations in the areas of Architectural and Industrial Coatings and help manufacturers to improve their cost competitiveness, quality and sustainability.

Being the world's leading chemical company, BASF supplies innovative and environmentally friendly raw materials to the manufacturers in the paints and coatings industry. With the acquisition of Ciba, our product portfolio has expanded significantly and covers products ranging from resins to additives, pigments, dispersions, solvents, acrylates & intermediates.

The portfolio also encompasses environment friendly dispersions, lead-free pigments, oxygenated solvents and intermediates like Propylene Carbonate for architectural, automotive & industrial coatings, which reinforce our commitment to grow sustainability in the Paints & Coatings industry.

List of the major public companies that compete in this industry

- Asian Paints
- Kansai Nerolac
- Berger Paints

Competition

Name	Last Price	Market Cap. (Rs. cr.)	Sales Turnover	Net Profit	Total Assets
Asian Paints	674.75	64,721.87	10,418.78	1,169.06	3,640.44
Berger Paints	353.95	12,263.91	3,384.82	234.25	1,434.69
Kansai Nerolac	1,851.00	9,975.40	3,154.40	206.60	1,474.91

Paint Sector Analysis:

The paint industry is expected to grow at 12-13% annually over the next five years from Rs 280 bn in FY13 to around Rs 500 bn by FY18. FY13 was a challenging year for the industry as a whole due to subdued demand across key sectors and rising inflation.

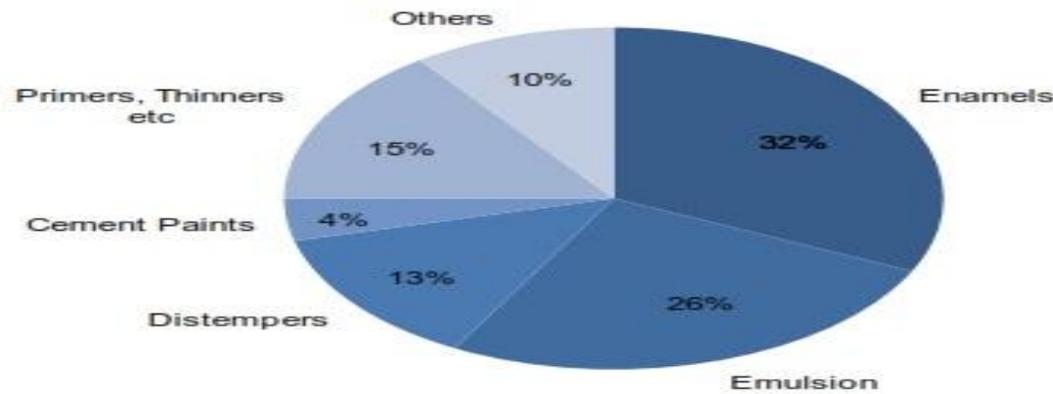
The unorganised sector controls around 35% of the paint market, with the organised sector accounting for the balance. In the unorganised segment, there are about 2,000 units having small and medium sized paint manufacturing plants. Top organised players include Asian Paints, Kansai Nerolac, Berger Paints and ICI.

Demand for paints comes from two broad categories:

- ❖ **Decoratives:** Major segments in decoratives include exterior wall paints, interior wall paints, wood finishes and enamel and ancillary products such as primers, putties etc. Decorative paints account for over 77% of the overall paint market in India. Asian Paints is the market leader in this segment. Demand for decorative paints arises from household painting, architectural and other display purposes. Demand in the festive season (September-December) is significant, as compared to other periods. This segment is price sensitive and is a higher margin business as compared to industrial segment.
- ❖ **Industrial:** Three main segments of the industrial sector include automotive coatings, powder coatings and protective coatings. Kansai Nerolac is the market leader in this segment. User industries for industrial paints include automobiles engineering and consumer durables. The industrial paints segment is far more technology intensive than the decorative segment.

The paints sector is raw material intensive, with over 300 raw materials (50% petro-based derivatives) involved in the manufacturing process. Since most of the raw materials are petroleum based, the industry benefits from softening crude prices.

Decorative Paints segment product break-up



Portor 5 Forces:

Supply: Supply exceeds demand in both the decorative as well as the industrial paints segments. Industry is fragmented.

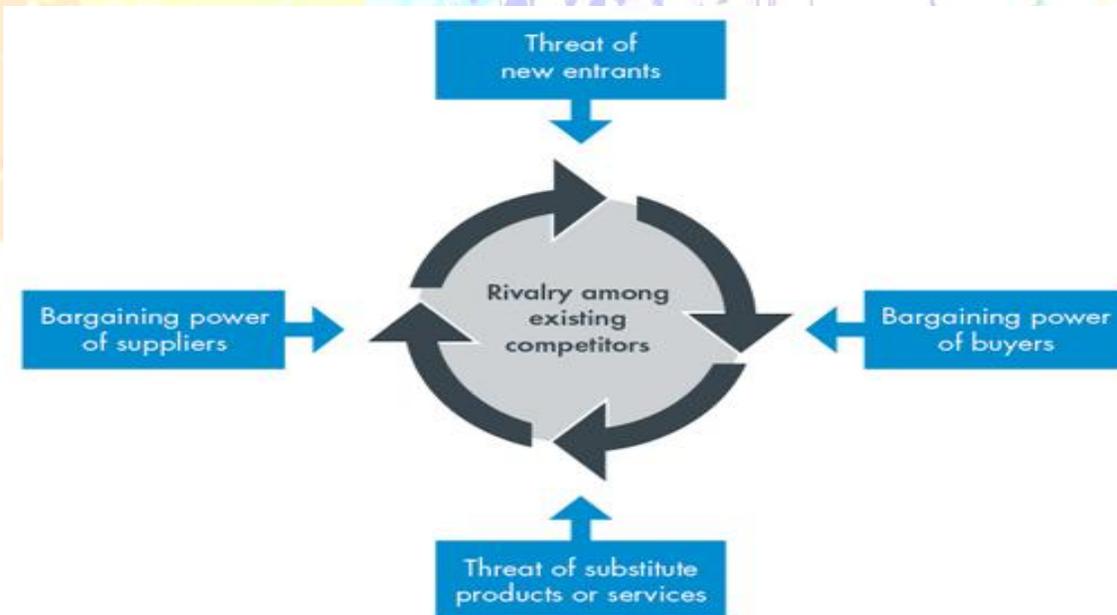
Demand: Demand for decorative paints depends on the housing sector and good monsoons. Industrial paint demand is linked to user industries like auto, engineering and consumer durables.

Threat of new entrants: Brand, distribution network, working capital efficiency and technology play a crucial role.

Bargaining power of suppliers: Price increase constrained with the presence of the unorganised sector for the decorative segment. Sophisticated buyers of industrial paints also limit the bargaining power of suppliers. It is therefore that margins are better in the decorative segment.

Bargaining power of customers: High due to availability of wide choice.

Rivalry among existing competitors: In both categories, companies in the organised sector focus on brand building. Higher pricing through product differentiation is also followed as a competitive strategy.



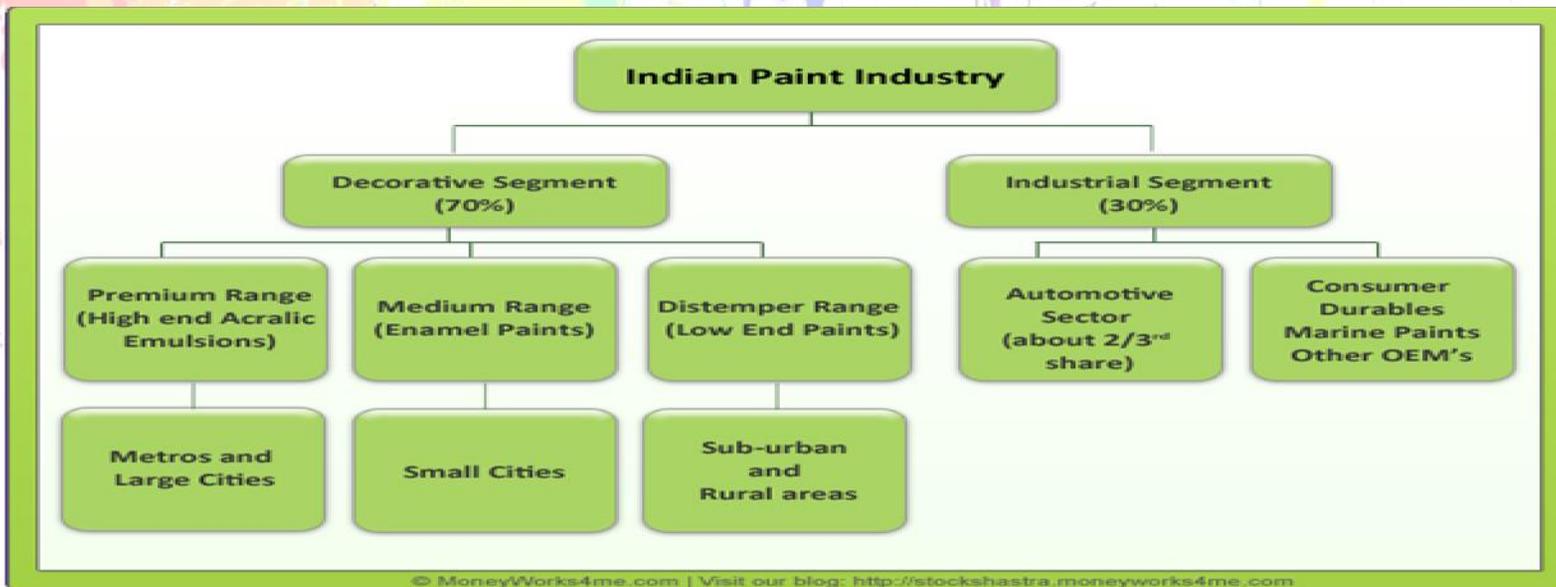
Financial Year '13

FY13 was a mixed bag for the paint companies. While all the 3 players viz. Asian Paints, Kansai Nerolac and Berger Paints reported a strong growth in sales, operating margins came under severe pressure due to raw material price inflation. Top-line growth was boosted by strong demand from the rural markets. Nonetheless, the demand environment in the industrial segment continues to remain challenging due to hawkish interest rate environment.

Performance on the margins was impacted by the rising prices of crude oil and titanium dioxide which increased the overall expenditure, thereby impacting profitability growth. However, companies are undertaking a gradual and calibrated price increase in order to shield margins. Nonetheless, as a complete pass on of raw material price increase is not possible in the industrial segment, the blended margins continue to suffer.

However, a good monsoon this year is expected to boost demand in the rural areas. A good harvest and festival season demand can boost volumes in the second half of FY14.

All the key players are in an expansion phase. Asian Paints' plant in Khandala, Maharashtra has recently got commissioned. Kansai Nerolac's capacity expansion plans at Jainpur and Bawal has culminated. Berger Paints has also undertaken capacity expansion for its plants located in Andhra Pradesh (AP). Further, expansion of water based plant at Rishra and Goa is also on track. As per estimates, paint capacities are expected to go up by 50-70% in the coming 3 to 5 years.



GDP relation:

GDP Growth to Revive Fortunes of Paint Industry

There is a high correlation between the paint industry's growth and GDP growth rate (as per our calculations, the correlation between Asian Paints' volume growth and India's GDP growth rate is a strong 0.76x)—paint industry volumes grow 1.5-2.0x India's GDP. We anticipate GDP to surge to 7.5% (5.4%, 6.3% and 7.5% in FY15, FY16 and FY17) riding on a new stable and business-friendly government in the saddle at the Center. Hence, we anticipate the paint industry to grow at a much faster pace. We estimate 11%, 13% and 15% YoY volume growth for Asian Paints in FY15, FY16 and FY17, respectively.

Table 1: Positive correlation between paint industry and GDP

Income Level	Increase in GDP will increase standard of living. With rise in income level, consumers will increase consumption which in turn will help the decorative segment.
Housing Sector	Growth in housing sector will increase urbanisation, provide cheaper loans and shift from semi – permanent to permanent housing structures will increase spending in the decorative segment.
Industrial Segment	The industrial segment can be further broken down into protective, general industrial, automotive powder and marine coatings. This segment accounts for 25% of the paint industry's revenue.
Infrastructure Investment	New projects in roads and ports will increase revenues of paint industry and drive the industrial segment.

Revival in GDP growth positive for paint industry



Industries Big Guns:

➤ Asian Paints:

Asian Paints is one of the best discretionary plays on macro recovery given that paint volumes surge a healthy 1.5-2.0x GDP. Moreover, decisive policy measures by the new business-friendly government will spur urban demand. Diversification into water proofing, modular kitchens and bath fittings places the company in a sweet spot to corner higher wallet share (Masco Corp in US has done this successfully). With 22% EPS CAGR, 347bps RoCE spurt over FY14-17E and metamorphosis into a home décor company, we anticipate valuations to remain rich.

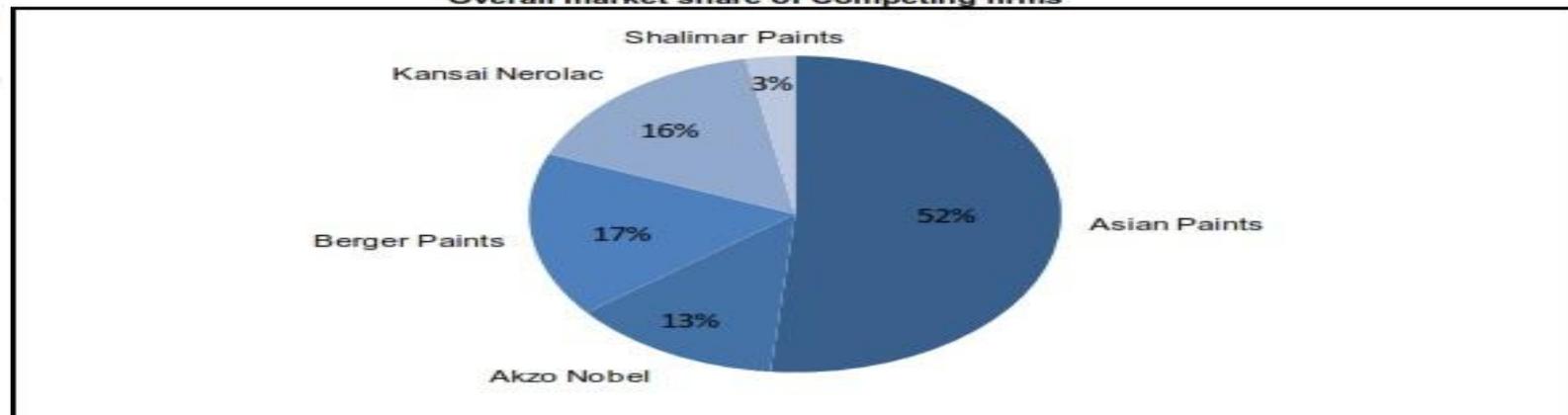
➤ Berger Paints:

Berger Paints (Berger) is the second largest paint company in India after Asian Paints. The company has a strong brand name with brands like *Berger Easy Clean*, *Silk*, *Rangoli*, *WeatherCoat* etc. The company has a strong distribution network of ~16,500 dealers and has ~12,000 tinting machines. As far as international operations are concerned, Berger has presence in Russia where it has a production facility with a manufacturing unit in Krasnodar. The company entered Nepal in 2000 when it acquired Jenson & Nicholson. It has also acquired Bolix SA of Poland and also tied up with Becker of Sweden. In 2013, Berger acquired the decorative business of Sherwin Williams India. Berger recently commissioned its Hindupur plant (total capacity of 300,000kl) in Andhra Pradesh and will increase its capacity in a phased manner.

➤ Kansai Nerolac

Kasai Nerolac is the third largest decorative paint company in India. The company has good brand strength, particularly in the interior paints segment with brands like *Nerolac Impressions*, *Nerolac HD* etc. It has high exposure to the industrial paints segment (~45% contribution), which has resulted in the company's subdued performance. The company has taken significant initiatives to improve revenue from the decorative business. It recently launched HD paints under *Nerolac* and was the first player to launch eco-friendly Zero VOC, low VOC, low odour range of decorative paints.

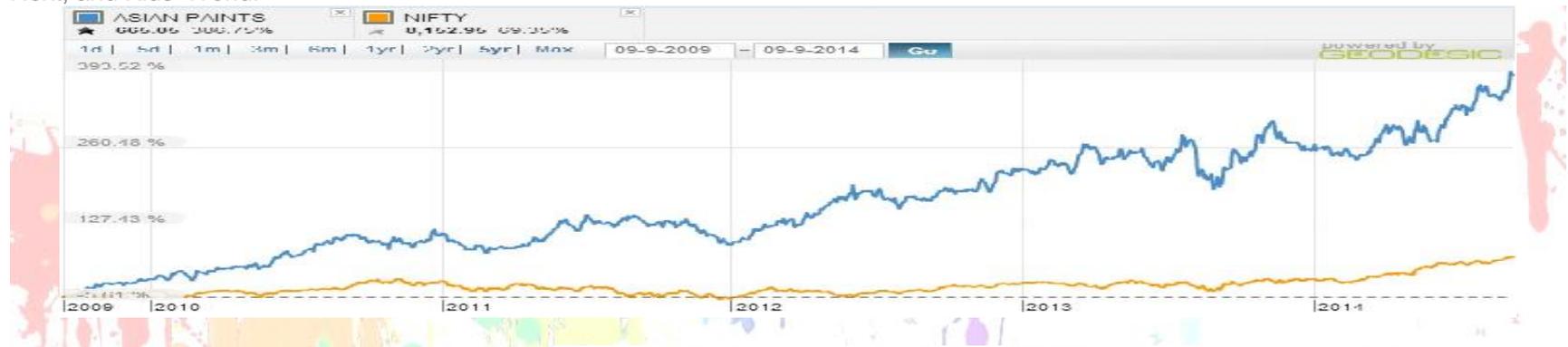
Overall market share of Competing firms



Asian Paints:

Since its foundation in 1942, Asian Paints has come a long way to become India's largest and Asia's third largest paint company, with a turnover of Rs. 127.15 billion. Asian Paints operates in 17 countries and has 23 paint manufacturing facilities in the world servicing consumers in over 65 countries.

Asian Paints has always been a leader in the paint industry, pushing new concepts in India like Colour Worlds, Home Solutions, Colour Next, and Kids' World.



MARKET CAP (RS CR)	63,340.63	*EPS (TTM)	12.45
*P/E	53.04	*P/C	45.04
*BOOK VALUE (RS)	37.54	*PRICE/BOOK	17.59
DIV (%)	530.00%	DIV YIELD.(%)	0.80%
MARKET LOT	1	FACE VALUE (RS)	1.00
INDUSTRY P/E	51.48	DELIVERABLES (%) ⓘ	54.67

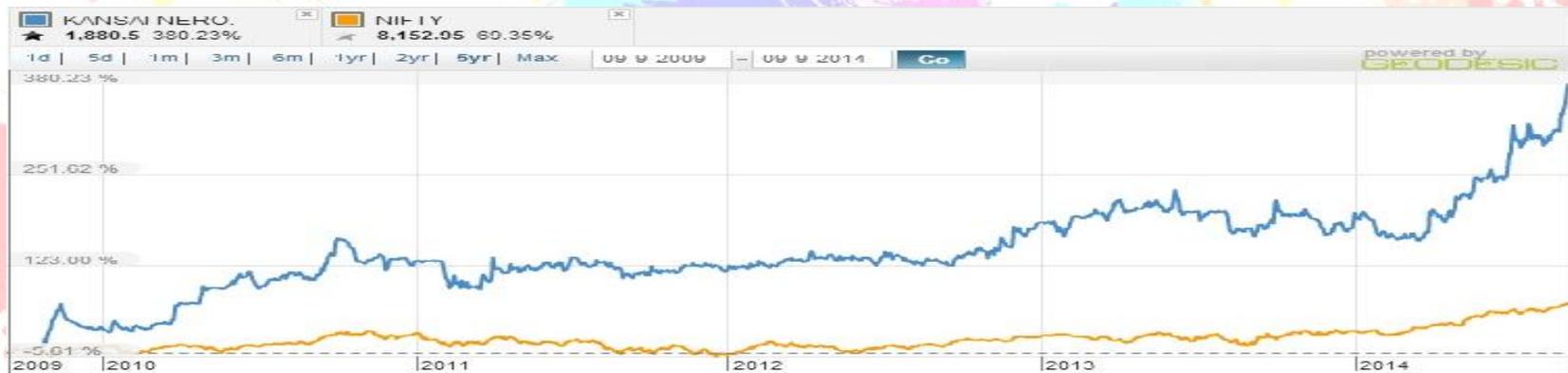
*Based on standalone numbers

Kansai Nerolac:

What has made Kansai Nerolac the second largest paint company in India?

It could be our product innovations, cutting-edge R&D, state-of-the-art solutions or our sensitivity towards the environment. Or it could be something that's a lot simpler, like our immense curiosity and unwavering belief in constant innovation.

As a result, today, Kansai Nerolac is the second largest coating company in India and a market leader in Industrial Coatings.



**KANSAI
NEROLAC**
PAINTS LIMITED

MARKET CAP (RS CR)	10,299.29	*EPS (TTM)	40.58
*P/E	47.09	*P/C	36.31
*BOOK VALUE (RS)	264.08	*PRICE/BOOK	7.24
DIV (%)	110.00%	DIV YIELD.(%)	0.58%
MARKET LOT	1	FACE VALUE (RS)	10.00
INDUSTRY P/E	51.48	DELIVERABLES (%)	94.60

* Based on standalone numbers

Berger Paints:

The driving forces of Berger Paints - reflect the very spirit of its founder Lewis Berger - who laid the foundations of brand Berger way back in 1760 in the UK. With modest beginnings in India in 1923, today, Berger Paints India Limited is the second largest paint company in the country with a consistent track record of being one of the fastest growing paint company, quarter on quarter, for the past few years.



MARKET CAP (RS CR)	12,328.01	*EPS (TTM)	6.97
*P/E	51.05	*P/C	41.09
*BOOK VALUE (RS)	32.67	*PRICE/BOOK	10.89
DIV (%)	110.00%	DIV YIELD.(%)	0.62%
MARKET LOT	1	FACE VALUE (RS)	2.00
INDUSTRY P/E	51.48	DELIVERABLES (%) ⓘ	40.42

* Based on standalone numbers

Future Prediction:

The paint industry estimated to double by 2016: Leading players hopeful

AC Nielsen in its latest report based on the data available on the coating industry for the year 2011-12 has valued the Indian paint industry at Rs 26,000 crore with 71 per cent of it being decorative paints and the remaining being industrial.

In volume terms, the size of the industry is 3.1 million tonnes with decorative paints being 2.4 million tonnes and industrial paints being 0.7 million tonnes. The per capita paint consumption has been estimated to be 2.57 kgs.

The paint market is estimated to double to Rs 50,000 crore by 2016 with per capita consumption increasing to over 4 kgs. Industry leaders are hopeful of achieving the ambitious growth over the next four years.

The growth in the market is going to be driven by emergence of the middle class in India, increase in the propensity to spend and growing young population tending to stay in nuclear families.

The demand for industrial paint is going to be driven by the pick-up in the automobile industry and growth in infrastructure in a country like India. "Infrastructure is at the lowest level in the country today, hence we see a sustained growth in the industrial paints business", said H M Bharuka, managing director, Kansai Nerolac Paints.

Prospect:

The market for paints in India is expected to grow at 1.5 times to 2 times GDP in the next five years. With GDP growth expected to be between 5-6% levels, the top three players are likely to clock above industry growth rates in the future, considering they have a strong brand and good reach.

Decorative paints segment is expected to witness higher growth going forward. The fiscal incentives given by the government to the housing sector have immensely benefited the housing sector. This will benefit key players in the long term.

Although the demand for industrial paints is lukewarm it is expected to increase going forward. This is on account of increasing investments in infrastructure. Domestic and global auto majors have long term plans for the Indian market, which augur well for automotive paint manufacturers like Kansai Nerolac and Asian-PPG. Increased industrial paint demand, especially powder coatings and high performance coatings will also propel topline growth of paint majors in the medium term.

If the new capacities do not get utilized well, companies may face margin pressures in the near term.

Recommendation:

We are bullish on the Paint Industry looking at both Top-Down and Bottom-Up Approach. Hence we Rank the companies captured as follows:

1. Asian Paints
2. Berger paints
3. Kansai Nerolac

We recommend these stocks with a long term view!!



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