Volume No. X Issue No. 06 **4 January, 2019**

S H Kelkar and Company

Rs 171

Set to regain its fragrance

BSE Sensex: 35,695 Nifty-50: 10,727

FINANCIALS: CONSOLIDATED

	SALES	OPM (%)	OP	OTHER INC.	PBIDT	INTEREST	PBDT	DEP.	PBT	EO	PBT AFTER EO	TOTAL TAX	PAT	EPS* (RS)
1603 (12)	924.87	15.7	144.97	10.45	155.42	15.42	140	29.7	110.3	0	110.3	37.24	73.06	5.1
1703 (12)	980.51	16.9	165.83	11.55	177.38	5.16	172.22	19.44	152.78	0	152.78	47.96	104.82	7.2
1803 (12)	1025.11	15.8	162.21	21.61	183.82	3.97	179.85	23.84	156.01	12.85	143.16	50.58	92.58	7
1903 (12P)	1213.52	14.1	171.26	23.32	194.58	7.4	187.18	29.75	157.43	0	157.43	46.62	110.81	7.7
2020 (12P)	1395.55	15.5	216.31	23.5	239.81	8.88	230.93	35.11	195.83	0	195.83	62.66	133.16	9.2

* Annualized on current equity of Rs 144.62 crore. Face Value: Rs 10 each. (P): Projections. Figures in Rs crore. *Source: Capitaline Databases*

S H Kelkar and Company (SHK) is the largest Indian-origin Fragrance & Flavour Company in India. It has a long standing reputation in the fragrance industry developed in 96 years of experience.

The Company offers products under SHK, Cobra and Keva brands.

The company operates in two segments: Fragrances, which manufactures/trades in Fragrances and aroma ingredients for Fragrances, and Flavours, which manufactures/ trades in Flavors.

Its manufacturing facilities are located at Vashivali, Vapi and Mulund in India, and Barneveld in the Netherlands.

It also conducts consultancy, formulation and efficacy studies in cosmetics and pharma products, and provides problem solving services for domestic and international markets.

Strong positioning

Favourable macroeconomic factors like growing disposable income, preference towards personal wellness products and increased confectionery and bakery sales have raised the demand for the Indian fragrance and flavour industry.

Further, increased penetration of FMCG products in rural areas, premiumisation of personal care and cosmetic products and higher demand for processed foods are other driver of growth.

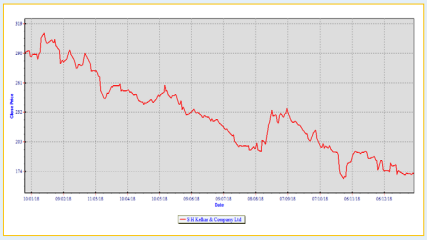
The size of the Indian fragrance and flavours market is estimated to be Rs 55.2 billion and is expected to grow at 10.2% CAGR over the coming five years. The fragrance market was estimated at Rs 27.5 billion in 2017, whereas the flavours market stood at Rs 27.7 billion during the same period.

Keva accounts for ~12.4% of the total fragrance and flavours market. In the fragrance market, it enjoys 23% market share; while in flavours, its market share stands at 2.3%.

One of India's largest fragrance players catering to wide range of industries

As one of India's largest fragrance player, it offers the ideal fragrant solution for every market, catering to the aspirational needs of new-age consumers around the world.

Some of the fragrances developed by the company decades ago have stood the test of time to find global appeal even today, underlining its creative strength and world-class processes.



STOCK DATA

BSE Code	:	539450
BSE Group	:	B
NSE Code	:	SHK
Bloomberg	:	SHKL IN
Reuters	:	SHKE BO
Par Value	:	Rs 10
52-week High/Low	:	Rs 314 / Rs 166
Sector	:	Chemicals

SHAREHOLDING PATTERN*

Category		% of equity
Foreign	:	30.76
Institutions	:	2.14
Govt Holding	:	–
Corporate Holding	:	4.75
Promoters	:	56.74
Public & Others	:	5.61
Total	:	100

* as on 30 Sep 2018
Source: Capitaline Databases

It offers fragrances in various categories, such as personal care, hair care, skincare and cosmetics, fabric care, household products and fine fragrances.

The company also offers flavors in various categories, such as dairy products, beverages, confectionery, bakery products and pharmaceuticals.

Management is confident of capitalizing on the potential

The management feels that the fragrances and flavours industry is in the midst of fast-paced growth and evolution. Growing demand, triggered by private consumption growth and a more aspirational consumer-driven environment, is catalysing a whole new level of churn in the domestic and global markets for fragrances, flavours and ingredients.

The management through its annual report has informed that the sectoral opportunity is burgeoning at a never-before speed, leading to the creation of a new set of game-changing realities in the industry, which the management is moving energetically to leverage, on the back of its intrinsic strengths and host of focussed initiatives.

Led by a future-centric strategic approach, the company is continuously surging forward, weathering the headwinds of today to find new avenues of growth and expansion in the key markets of its focus, across India, South East Asia and Europe.

With its strong understanding of the evolving consumer demands, the management is cognizant of the need to continue persistently to channelise enduring growth that will sustain for a long time to come.

The management believes that the path to sustainable growth lies in visionary thinking coupled with dynamic functionality – a combination it is proud to own with the legacy experience of the promoters combining with the youthful energy of its professional management team.

In line with its futuristic growth strategy, the management has built the fundamentals to provide the platform for driving growth, through a concerted thrust on innovation, discovery, resource and sourcing. At the same time, it has been steadfastly focused on robust inventory planning, backed by consistent efforts to align its organic with inorganic growth philosophy and a cautious but targeted approach in terms of geographic expansion.

Within India, it is focusing on key high potential accounts in the North Indian markets as part of its expansion strategy. The company intends to identify similar opportunities in other markets, where it expects the opportunity landscape to expand in the coming years. It is focused on going forward speedily into new markets of growth wherever it sees them opening up.

It is now moving forward at a more accelerated pace to seize the opportunities that it sees across sectors and geographies.

The management believes that it has the capabilities needed to sustainably outperform the sector growth rates for years to come with the strength of its industry position and unique business model.

Strategic acquisitions have lent the necessary synergies

Its strategic acquisitions have lent the necessary synergies to further propel growth agenda in the segments of its focus – namely Fabric Care, Air Care and Fine Fragrances, which it has identified for vertical growth.

Based on the opportunity matrix, the management has decided to focus on the

S H Kelkar and Company (SHK) is the largest Indian-origin Fragrance & Flavour Company in India. It has a long standing reputation in the fragrance industry developed in 96 years of experience

The size of the Indian fragrance and flavours market is estimated to be Rs 55.2 billion and is expected to grow at 10.2% CAGR over the coming five years

three key regions of South Asia (through India), South East Asia (through Indonesia) and Western Europe (through Italy). It sees significant opportunities in these markets across various product lines, particularly Air Care, Fabric Care and Fine Fragrances.

The management believes that this focused strategy will enable it to map products even more powerfully to consumer aspirations, while balancing traditional philosophy with contemporary market needs.

Its strategic acquisitions are aimed at putting it on the fast trajectory of growth by giving it a leverage in the products, segments and geographies across. It is, at the same time, a power engine of premiumisation strategy, which will lead to incremental value growth in the coming years.

The acquisition of Creative Flavours & Fragrances SpA (CFF), an Italian company headquartered in Milan, endorsed this strategy.

With the acquisition, which took place in January 2018, it has acquired 51% ownership stake in CFF, which is one of the top five players in the Italian market today and is engaged in the production and sale of fragrances.

This bolt-on acquisition will open new avenues for the company to expand product offerings in its key focus areas of Fine Fragrances and Fabric Care. It will also give the company access to new markets in Western Europe, as well as to premium customers and global talent, thus creating a bigger platform for growth of market share and leadership position in the global Fragrance industry.

The management believes this acquisition, along with its Fine Fragrance Studio in Amsterdam, will strengthen its strategy to expand presence and product offerings in focused growth areas.

In combination with the acquisition of Fragrance Encapsulation Technology from Tanishka, this also gives the company a strong platform for Fabric Care development by providing it with a ready library for fabric care and home care, for use in markets, particularly India, Indonesia and the Middle East.

Consolidated performance sees comeback in Q2

In the last couple of quarters the company was faced with sharp rise in raw prices, shortage of some key raw materials, forex volatility and some demand slowdown due to GST related and client issues. However the worst seems to be over and the company has already shown signs of regaining growth momentum from September 2018 quarter.

In September 2018 quarter, it registered 28% rise in consolidated sales to Rs 284.50 crore. OPM fell 270 basis points to 13.3% which saw OP rise 6% to Rs 37.72 crore. Other income jumped 334% to Rs 5.04 crore and interest grew 78% to Rs 1.89 crore. After providing for depreciation (up 33% to Rs 7.58 crore), PBT went up 12% to Rs 33.29 crore.

Tax fell 56% to Rs 4.88 crore (due to deferred tax credit of Rs 12.06 crore against Rs 3 lakh), after which PAT went up 51% to Rs 28.41 crore.

For the six months, it registered 19% rise in consolidated sales to Rs 521.90 crore. OPM fell 390 basis points to 13.7% which saw OP fall 8% to Rs 71.67 crore. Other income grew 32% to Rs 7.32 crore and interest grew 104% to Rs 3.40 crore. After providing for depreciation (up 25% to Rs 14.35 crore), PBT went down 12% to Rs 61.24 crore.

Tax fell 39% to Rs 14.88 crore (due to deferred tax credit of Rs 12.07 crore against provision of Rs 62 lakh), after which PAT went up 2% to Rs 46.36 crore.

Keva accounts for ~12.4% of the total fragrance and flavours market. In the fragrance market, it enjoys 23% market share; while in flavours, its market share stands at 2.3%

Growing demand, triggered by private consumption growth and a more aspirational consumer-driven environment, is catalysing a whole new level of churn in the domestic and global markets for fragrances, flavours and ingredients

Fragrance division delivered a healthy growth in H1 assisted by robust revival in the second quarter. In H1 FY19, Domestic fragrance business reported growth of 24% while overseas revenues grew by 3%.

In Q2 FY19, the domestic fragrance delivered a strong growth of 36%, translating into a consolidated segment growth of 31%. The overseas division also marked robust growth of 20%.

In H1 2019 Flavor division, revenue fell 9%. The domestic business in particular de-grew by 20% while overseas marked a growth of 12%. During Q2 FY19, increased momentum has registered a healthy 24% growth in overseas business. The domestic segment during the quarter de-grew by 3%.

Raw material cost pressure continued to impact profitability in both the segments. However company has already taken steps in passing on the higher cost of raw materials by raising product prices and started captive production of some raw materials to reduce shortages in availability. This should help in improved show in H2FY19.

Operationalization of Mahad plant, one of the largest manufacturing plant for Tonalid worldwide

The company formerly inaugurated aroma ingredients unit at Mahad during September 2018 quarter. This plant has a total installed capacity of 1,200 metric per annum and is one of the largest manufacturing plant for Tonalid worldwide. The state-of-art facility will manufacture Tonalid and other key raw materials used in the fragrance industry.

The commissioning is in sync with previously announced strategic investment to shift production of Netherlands to a high quality operating efficient center in India. Additionally, it has optimized capacity in other Tonalid manufacturing facility, which it acquired as Anhui in China at a nominal capex. The installed capacity of this Tonalid plant has been expanded to 400 metric tons from 300 metric tons at the time of acquisition.

Outlook

On the whole, the company is witnessing a healthy revival in the demand environment and improved consumption pattern across domestic and international markets. The new product launches, particularly in FMCG industry, is showing robust traction and an improved macro environment, SHK is focusing on deepening its customer engagement and adding new products to positively impact growth, especially in the fragrance division. This, along with improving availability of key ingredients will enable it to further strengthen business performance from the second half of the current fiscal.

Consumer inclination towards natural fragrances is an advantage for Indian manufacturers of ingredients and blends, as the country is rich in raw materials.

Valuation

In FY 2019 we expect the company to register consolidated EPS of Rs 7.7, which can go up to Rs 9.2 in FY2020. The stock trades at Rs 171. P/E works out to 18.8.

The company is continuously surging forward, weathering the headwinds of today to find new avenues of growth and expansion in the key markets of its focus, across India, South East Asia and Europe

Raw material cost pressure continued to impact profitability in both the segments. However company has already taken steps in passing on the higher cost of raw materials by raising product prices and started captive production of some raw materials to reduce shortages in availability

S H KELKAR AND COMPANY: CONSOLIDATED RESULTS

	1809(3)	1709(3)	VAR.(%)	1809(6)	1709(6)	VAR.(%)	1803(12)	1703(12)	VAR.(%)
Sales	284.50	221.93	28	521.90	438.99	19	1025.11	980.51	5
OPM (%)	13.3	16.0		13.7	17.7		15.8	16.9	
OP	37.72	35.44	6	71.67	77.57	-8	162.21	165.83	-2
Other inc.	5.04	1.16	334	7.32	5.53	32	21.61	11.55	87
PBIDT	42.76	36.60	17	78.99	83.10	-5	183.82	177.38	4
Interest	1.89	1.06	78	3.40	1.67	104	3.97	5.16	-23
PBDT	40.87	35.54	15	75.59	81.43	-7	179.85	172.22	4
Dep.	7.58	5.70	33	14.35	11.52	25	23.84	19.44	23
PBT	33.29	29.84	12	61.24	69.91	-12	156.01	152.78	2
EO	0.00	0.00	—	0.00	0.00	—	12.85	0.00	-100
PBT after EO	33.29	29.84	12	61.24	69.91	-12	143.16	152.78	-6
Total Tax	4.88	10.98	-56	14.88	24.25	-39	50.58	47.96	5
PAT	28.41	18.86	51	46.36	45.66	2	92.58	104.82	-12
EPS (Rs) *	7.9	5.2		6.4	6.3		7.0	7.2	

* Annualized on current equity of Rs 144.62 crore. Face Value: Rs 10 each. (P): Projections. Figures in Rs crore.
Source: Capitaline Databases