



**Dynemic Products Ltd (BSE Code: 532707) – Alpha/Alpha + stock  
report for Mar'16**

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## Company Snapshot (21<sup>st</sup> Mar'16)

**Rating** – Positive – 3% weightage; this is not an investment advice (refer rating interpretation), the rating is only for indicative purpose and please take your own decision regarding the same.

**BSE CMP** – 46.70

**Dividend yield** – 3.20%

**BSE Code** – 532707

**Market capitalization** – Rs 52.90 cr.

**Total Equity shares** – 1.10 cr.

**Face Value** – Rs 10.00

**52 Weeks High/Low** – Rs 79.00/39.00

Particulars (in cr.)	FY 09	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15
Income from operations	50.07	63.75	64.96	82.93	85.76	116.36	128.35
Total Cost of Goods sold	32.99	37.99	36.61	48.24	51.73	66.51	73.08
Gross profit	17.08	25.76	28.35	34.69	34.03	49.85	55.27
Gross Profit margin (%)	34.11%	40.41%	43.64%	41.83%	39.68%	42.84%	43.06%
EBITDA	6.01	10.38	10.79	10.92	9.28	18.64	17.8
EBITDA margin (%)	12.00%	16.28%	16.61%	13.17%	10.82%	16.02%	13.87%
Other Income							
Div/interest/other	-0.40	0.35	0.43	0.29	0.73	0.37	0.28
Exchange variation/Sale of asset							
Depreciation	-0.96	-1.45	-1.50	-1.63	-1.75	-1.81	-3.02
Interest	-1.46	-1.77	-1.24	-1.60	-1.56	-1.36	-2.24
PBT	3.18	7.52	8.48	7.98	6.68	15.83	12.82
PAT	1.90	4.85	5.71	5.29	4.33	10.23	9.34
ROAE	6.94%	16.62%	17.52%	14.60%	11.01%	22.85%	17.50%
Cash flows from operations	5.08	-0.69	6.06	-0.05	4.85	6.61	-1.24
Debt to Equity ratio	0.53	0.54	0.42	0.54	0.49	0.51	0.56
Net debt	14.74	16.69	14.54	20.42	20.06	25.16	32.6

## Introduction

Dynemic Products is a small company and we see this company as a medium term statistical bargain around current levels of 40-50. The stock is currently quoting around 50 crores market cap with 3 years average net profit of 8.8 crores and thereby PE of 5.9 and trailing twelve months PE of 6.9. The stock also offers ~3.2% dividend yield.

Further, though promoter holding is moderate at ~39%, they have been continuously making market purchases and increasing their holding in the company around current levels.

## Understanding Business and Company

Dynemic Products is one of India's leading manufacturers and exporter of complete range of Food colours, Lake colours, Blended colours, & US-FDA certified FD&C colours & Dye Intermediates. The company's products are used widely in food & beverages, drugs, cosmetics and personal care products.



The products manufactured by Dynemic meet the regulatory requirements of BIS, EU, FDA, WHO and also it meets the criteria of Kosher & Halal Certification. As can be checked at the following [LINK](#), Dynemic is one of the few Indian companies to be certified by US-FDA.

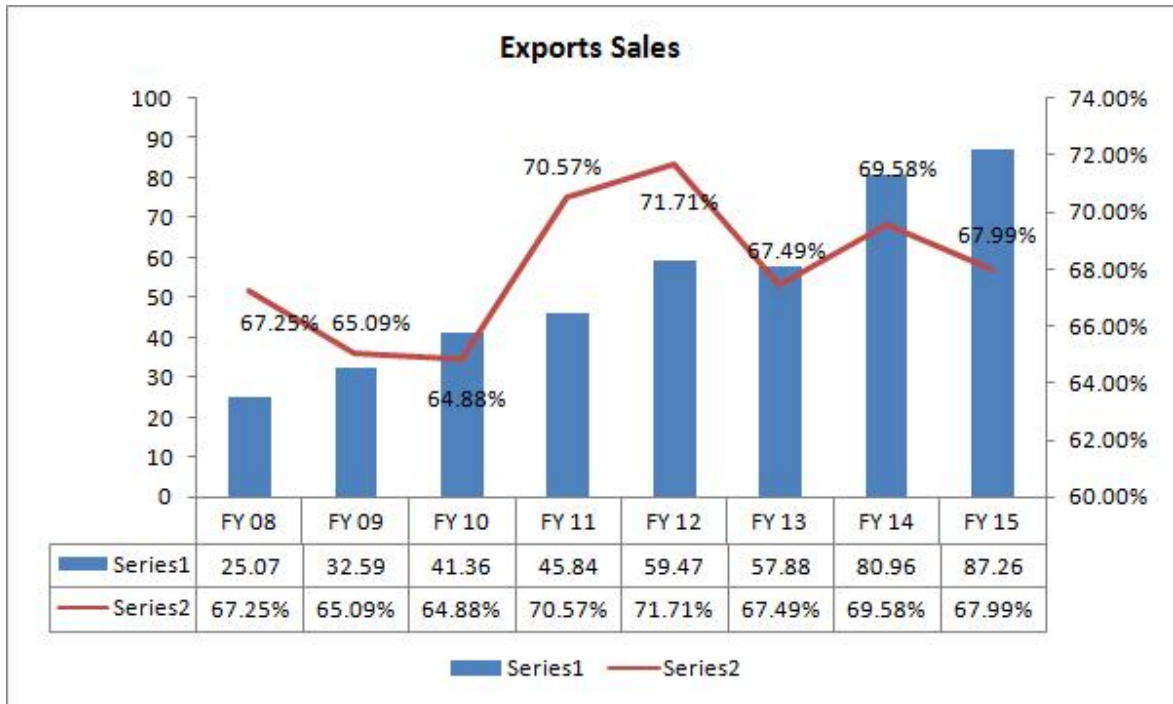
Also, as can be checked at the link, there are only 6 Indian companies including Dynemic Products that are approved by US-FDA for foods, drugs, cosmetics colour additives.

**Synthetic food colours applications** - Synthetic food colours are used to enhance the original colours associated with a given product. Due to light, air, temperature and moisture, product's colour tends to fade or disappear, so synthetic colours are added.

Primary Food Colours are easily soluble in water and have wide application like in Foodstuff, Beverages, Animal feeds, Sea-Foods, Meat & Fish products, Cosmetics, Toiletry products etc.

Lake Colours are dispersible in vegetable oil, and can be mixed with fats, oils, etc. As they are more stable than water-soluble colours, they are widely used in cosmetic and pharmaceutical industry.

**Exports** – Dynemic is largely an exporter of food colours with ~67% of its sales coming from regions outside India. There has been a notable transition in the global arena during the last 2-3 decades in the manufacturing base of colorants, with a shift in production from Europe, USA and Japan to Asia viz. China, India, Taiwan, Thailand and Indonesia etc. With decline in production in most of the traditional centers, non-traditional centers like India and China are now preferred sources for supply of colorants to the global market.



Source: Dynemic Products ARs

So, as can be observed the exports sales have been recording good growth and have grown from 25.07 crores in FY 08 to 87.26 crores in FY 15 and the contribution to the overall sales have remained steady at around 67%

What is interesting to note from the above illustration is that over the last 8 years the exports sales have remained in the range of 65%-72% of the entire sales of the company and therefore more or less both domestic and export sales have grown at similar pace.

**Manufacturing facilities** – In India, Gujarat and Maharashtra account for nearly 95% of the colorant production in the country and Dynemic also has its two plants spread over 50,000 sq. Mt of area in Ankleshwar, Gujarat. Further, Company also has a plot in Dahej - III Industrial Estate having plot area of 80000 sq. Mt., however pending government approvals has delayed expansion at Dahej.

Company is environmentally conscious and considering strict regulations it has installed Multiple Effect Evaporator Plant (MEE) water effluent plant in both the units for recycling maximum water waste.

## Food colors and dye-stuff industry

The colour of our food plays an important role by visually stimulating our appetite.

### **Why is Colour added in foods?**

- Off colour foods are generally considered inferior in quality and so colours are added.
- Colours can also protect vitamins and flavours that may be affected by sunlight during storage.
- By using colours, we can enhance the natural colour of a dish and introduce decorative colours to other foods.
- Colour of the food can influence the perceived flavour.

As a result Food & beverage manufacturers are resorting to natural and synthetic food colours to enhance the organoleptic appeal of the finished product. The rising preference for 'clean label' foods has enhanced the growth of the market. Food colourings are tested for safety by various regulatory bodies and institutions, globally. There are different regulations established by the government on the use of any particular set of synthetic food colours in their respective countries.

In the U.S., FD&C numbers (which generally indicate that the FDA has approved the colorant for use in foods, drugs, and cosmetics) are allotted to approve synthetic food dyes that are not found in nature; while in the European Union, E numbers are used for both synthetic and natural colorants. Food colour manufacturers are investing in new products and innovation technologies that impart a wide range of colours to the food and beverages.

The food colours market is growing with the increase in demand for food. This growth will be maintained in the future with finding new sources of raw materials, the launch of new products, and using advanced technologies for colour production. Globalization and the changing lifestyles have resulted in an increase in the usage of food colours in the developing markets, especially the Asian markets.

The demand for food colours is high in the developed markets of the U.S. and U.K. And the developing countries such as China, Australia, New Zealand, India, and the Latin American countries are projected to experience a strong increase in demand for food colours. Countries such as China and India that have abundant resources for raw materials and widely available cheap labour force provide great opportunity for the growth of the food colours market. Key players in this market are setting up their production units in these countries. Thus, it is projected that the market in this region will grow tremendously.

As per various estimates, China's share in dyestuff market is estimated to be around 25%, while India's share is about 5-7%, though continuously increasing year by year. Further, the complete group of China, Taiwan, India, Japan and Pakistan are among major dyestuff producing countries in the world. Production share of developed countries is expected to reduce further in the coming years.

Today, the thrust has shifted towards using environment friendly natural dyes. With many countries laying curbs against harmful dyes, the industry can prosper only if dyes are not hazardous and are environment friendly in nature.

**Level playing field between India and China** – One of the major challenges in the Dyes and Dyes intermediates business or in general in chemicals business is the compliance of Environmental norms. Over a period of time, the regulating agencies have become more stringent in ensuring the compliance of the environmental norms.

Two Western States viz. Maharashtra and Gujarat account for over 90% of the dyestuff production in the country. Several units, which were not complying with Pollution control norms have been shut down. This adds to the advantage of companies like Dynamic Products which follow norms.

In India, compliances were made stringent about 3 years back while in China the tighter compliances have been imposed since last year.



These compliances requires additional investments into ETP setup, which translates into increased costs for the manufacturers along with general increase in labor and other costs in China and India. Several units which were not complying with Pollution control norms have been shut down in both India and China.

This has resulted in level playing field for Indian companies and at a same time reduction in capacity utilization in China.

At the same time MNCs are de-risking their sourcing arrangement and want to add an Indian source, which is a major positive for Indian companies. This is being witnessed across Specialty chemicals including dyes and dyes intermediates.

## Management

Dynemic Products is basically a family run business with founder and promoter Mr. Bhagwan Das Patel as the Managing Director of the company. Other members of the family like Dashrath Patel, Ramesh Patel and Dixit Patel are also involved in day-to-day affairs of the company and are whole time Executive Directors.

In our view the promoters have been taking home reasonable remuneration with only the Managing Director charging commission based on the performance of the company.

The related party transactions also seem very much within reasonable limits.

Promoters seem to value equity and haven't diluted the same in the last more than 10 years.

### Shareholding pattern

	Dec'15	Sep'15	Jun'15
<b>Promoter and Promoter Group</b>	<b>38.34%</b>	<b>37.93%</b>	<b>37.77%</b>
India	38.34%	37.93%	37.77%
Foreign			
<b>Public</b>	<b>61.66%</b>	<b>62.07%</b>	<b>62.23%</b>
<b>Total</b>	<b>1,13,28,449</b>	<b>1,13,28,449</b>	<b>1,13,28,449</b>

From a passive investor's perspective it's important for the ones running the company to have high ownership as it aligns their interest in line with those of minority shareholders and in the case of Dynamic Products the promoters own reasonable stake at 38.34%

We generally prefer companies with promoter's stake of 50% or more, however what's working in favor of Dynamic is that promoters have been increasing stake through open market purchases and in general it's always a positive if promoters themselves are increasing stake in the company through open market purchases.

As on 31<sup>st</sup> Dec'15, the major shareholders of the company and their stakes are as below:

<b>Name of the shareholder</b>	<b>Category</b>	<b>% stake in Dynamic Products</b>
<b>Promoters and PAC</b>	Promoters	38.34%
<b>Dahyabhai Nathbhai Patel</b>	Public	2.61%
<b>Shashikant P. Patel</b>	Public	1.95%
<b>Sanjay Katkar</b>	Public	1.00%

As can be observed, institutional interest in the company is zero; if the company is able to perform consistently and grow its sales and profitability it will attract institutional interest and there could be re-rating in the valuations of the stock; however it will happen only over longer term.

## Dynemic Products – Performance Snapshot

Dynemic Products isn't the highest quality company; however it is still a reasonably well managed company that has demonstrated consistent growth and decent financial performance over the last several years.

Particulars (in cr.)	FY 09	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15
Income from operations	50.07	63.75	64.96	82.93	85.76	116.36	128.35
Total Cost of Goods sold	32.99	37.99	36.61	48.24	51.73	66.51	73.08
Gross profit	17.08	25.76	28.35	34.69	34.03	49.85	55.27
Gross Profit margin (%)	34.11%	40.41%	43.64%	41.83%	39.68%	42.84%	43.06%
EBITDA	6.01	10.38	10.79	10.92	9.28	18.64	17.8
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Exchange variation/Sale of asset							
Depreciation	-0.96	-1.45	-1.50	-1.63	-1.75	-1.81	-3.02
Interest	-1.46	-1.77	-1.24	-1.60	-1.56	-1.36	-2.24
PBT	3.18	7.52	8.48	7.98	6.68	15.83	12.82
PAT	1.90	4.85	5.71	5.29	4.33	10.23	9.34
ROAE	6.94%	16.62%	17.52%	14.60%	11.01%	22.85%	17.50%
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Debt to Equity ratio	0.53	0.54	0.42	0.54	0.49	0.51	0.56
Net debt	14.74	16.69	14.54	20.42	20.06	25.16	32.6

Some observations about the financial performance of the company are as below:

- The company has recorded 17.5% CAGR in sales for the last 10 years and 15.5% CAGR for the last 5 years.
- Both exports and domestic sales have been recording similar pace of growth as the contribution of exports hasn't changed much and remained in the range of 65-70%
- Despite being in the chemicals business where in general the pricing power is low, the company has been able to maintain its gross margins in the region of 40-43%
- The EBITDA has grown at 18% annualized for the last 10 years and 14% annualized for the last 5 years. Over the last 5 years the company has recorded EBITDA margins in the range of 11% and 16.5%.

- EBITDA margins of the company have been slightly cyclical and we believe with companies like Dynemic, it's probably better if one is entering the stock when the margins are at cyclical low.
- The before tax profitability has grown at a rate of 15% annualized for the last 10 years and ~13.5% annualized for the last 5 years.
- In terms of return ratios the company has been maintaining around 17% + return on average equity since the last 5-6 years.
- The operating cash flows after interest and tax payments have been positive across the years, though slightly lower than the reported profits and thereby company has been resorting to some amount of debt for capital expenditures.
- The debt equity ratio has consistently been below 0.50-0.55 and the same was 0.44 at the end of Sep'15.

Considering various financial parameters, we believe the performance has been good and more or less consistent over the years

**What's the way ahead?** The company has two manufacturing units in Ankleshwar, Gujarat. Further, it has been allotted a plot in Dahej - III Industrial Estate having plot area of 80000 sq. Mt.

The management intends to set up 3<sup>rd</sup> unit in Dahej and will undertake expansion in three phases; however as the industry is subject to very strict environmental norms, the government approvals are pending and therefore the company hasn't been able to start work on 3<sup>rd</sup> unit. Once they get the approval, they will begin with first phase of expansion.

As mentioned above, with regulatory strictness a lot of non-compliant units have been shut down in both India and China in the last few years, so to a certain extent it's an advantage for companies like Dynemic which have set up treatment plants and are environmentally conscious. At the same time, delays in government approvals for new units also hurt them.

While it is difficult to predict the time line for expansion, we believe FY 17 may again be flattish for company in terms of sales; however as soon as the first phase of the expansion is complete, we expect the company to resume 15-20% growth trajectory.

## Valuations

Dynemic Products isn't the highest quality company with strong moats, however what makes it attractive is that it's a reasonably well managed company that has demonstrated consistent growth and decent financial performance over the last several years and the fact that it is available at low valuations and the promoters have been increasing stake through open market purchases.

As mentioned above, around current price of 40-50 we find Dynemic Products as a statistical bargain opportunity from a medium term investment perspective.

The stock is currently quoting around 50 crores market cap with 3 years average net profit of 8.8 crores and thereby PE of 5.9 and trailing twelve months PE of 6.9. The stock also offers ~3.2% dividend yield.

## Dividend Policy

	<b>Dividend Payout ratio</b>				
	<b>FY 12</b>	<b>FY 13</b>	<b>FY 14</b>	<b>FY 15</b>	<b>FY 16</b>
<b>Dividend Per share (in Rs.)</b>	1.30	1.30	1.50	0	1.50
<b>Dividend Payout ratio</b>	27.78%	33.94%	16.61%	0%	~22.62%

Dynemic has been continuously paying dividend since 2007, however in 2015 it skipped dividend in order to conserve resources for further expansion.

In 2016 the company has again resumed dividend pay-out with Rs 1.50/- per share. At around current price the stock offers dividend yield of ~3.2%.

## Risks & Concerns

Dyes, dyes intermediate industries are subject to strict environmental laws; so any change in the environmental laws of the state or country of export can substantially impact the business of the company.

Exports account for 70% of the sales of the company and therefore unfavourable cross country currency fluctuations can negatively impact the performance of the company.

Company faces competition both from local and global players and since synthetic food colours are basically commodities, it doesn't benefit much from lower commodity prices as it has to pass on the same. Further, during inflationary period, there's a lag before which the company is able to raise the prices.

Natural food colours are increasingly gaining acceptance despite being expensive in comparison to synthetic food colours. Dynamic does have some presence in Natural food colours, however major sales are from synthetic colours and therefore natural food colours pose long term business risks to the company.

**Disclosure:** I don't have any investment in Dynamic Products Ltd.

Best Regards,

Ekansh Mittal

Research Analyst

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## Rating Interpretation

Positive – Expected Absolute return of over 20%

Neutral – Expected Absolute return in the range of +/- 20%

Negative – Expected Absolute return of over -20%

% weightage – allocation in the subject stock with respect to equity investments

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Analyst ownership of the stock: No

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A graph of daily closing prices of securities is available at <http://www.nseindia.com/ChartApp/install/charts/mainpage.jsp>, [www.bseindia.com](http://www.bseindia.com) and <http://economictimes.indiatimes.com/markets/stocks/stock-quotes>. (Choose a company from the list on the browser and select the "three years" period in the price chart

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