Aarti Industries Ltd — Nov 2024 Quarterly Analysis

1. VERDICT & BUSINESS QUALITY SNAPSHOT

The punchline. Read this first — it frames everything below.

Result: Miss (on Guidance) / Mixed (on Operationals) **One-line:** The thesis is undergoing a "Predictability Reset" as management significantly lowered FY25 guidance due to volatility in the new Energy (MMA) segment and prolonged China-led pricing pressure, shifting the recovery timeline to FY28.

Dimension	This Quarter	Signal / Evidence	Sentiment
Beat/Miss vs Guidance / Prior Quarter	Weak Miss	Q2 EBITDA (□202 Cr) declined 35% QoQ; FY25 guidance cut by ~40% vs earlier expectations.	□
Earnings Quality	Low (Volatility driven)	PAT aided by □2.3 Cr one-off divestment; MMA volumes dropped 34% in one quarter.	□
Guidance Confidence	Weak	Management admitted earlier MMA ramp-up assumptions were "over-optimistic."	□
Management Credibility	Neutral	New CEO (Suyog Kotecha) brings realism but inherits a "guidance walk-back" legacy.	□
Business Quality Signal	Deteriorating (Predictability)	Core chemistry is strong, but the shift to "Energy/Octane Boosters" introduces high-beta macro volatility.	□
Key Q&A Exchange	Q7 on Predictability	Analyst Archit (Barclays) challenged the 40% EBITDA guidance cut; Mgmt blamed MMA volatility.	□
The Street's Primary Anxiety	MMA Volatility & Cash Flows	Fear that AIL is becoming a volatile proxy for gasoline-naphtha spreads; Mgmt cites geography diversification.	□
Capital Cycle Stage	Investment	Massive capex (□1,300-1,500 Cr in FY25) continues while FCF remains negative.	□
Margin / Return Ratio Trajectory	Deteriorating	ROCE remains below the 15% target; EBITDA margins squeezed by China dumping.	□
Pricing Power	Eroding	China overcapacity in PDA/Agchem chains forcing AIL to accept "bottomed-out" pricing.	□
FCF Conversion & Quality	Weak	Capex > EBITDA; FCF negative for 3 years; Debt/EBITDA rising to ~3.3x.	□
Competitive Moat Signals	Stable	Integrated Benzene/Toluene chains and "only-in-India" Ethylation/Propylation capability intact.	□
Balance Sheet Strength	Adequate	Net Debt/EBITDA at 3.3x (vs 2.5x target); Capex guidance for FY26 reduced to □1,000 Cr.	□
Working Capital Efficiency	Deteriorating	Extended cycles in textiles/dyes; month-on-month volatility in energy contracts.	□
Mgmt Guidance Track Record	Unreliable	Frequent shifts in EBITDA targets (FY25 target reset from □1,500 Cr to ~□1,050 Cr).	□
Key Vulnerability / Red Flag	Energy Segment Exposure	37% of revenue is now linked to volatile gasoline-naphtha deltas outside management control.	□
Management Tone	Professional but Realistic	The new CEO is resetting expectations with a "consultant-style" focus on cost and ops.	□

Sentiment: □Negative

Key Takeaways: * **Positives:** Non-energy volumes grew 22% YoY, indicating strong demand recovery in Dyes, Pigments, and Polymers. The company is successfully diversifying away from Middle East concentration in MMA toward the US and Europe. New CEO onboarding signals a shift toward professionalized, execution-focused management. * **Negatives:** The massive walk-back on FY25 EBITDA guidance (from ~□1,500 Cr potential to □1,000-1,050 Cr) severely damages short-term credibility. The MMA business, once touted as a high-growth stable pillar, has proven to be highly volatile and linked to refining spreads. FCF remains negative as capex continues to outpace operating cash flows. * **Street Concern:** Analysts are primarily worried about the lack of earnings predictability and the continued high leverage (3.3x Debt/EBITDA). Management responded by cutting FY26 capex guidance and focusing on a □150-200 Cr cost-optimization program. * **Forward Watchpoint:** Track the gasoline-naphtha spread in Q3/Q4; if it stays compressed, the revised FY25 EBITDA guidance of □1,000+ Cr may still be at risk despite the "seasonal US demand" optimism.

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2. BUSINESS PERFORMANCE

2A. KEY METRICS

DATA SOURCE: PPT figures used as primary source. Concall used for Mgmt Commentary column and any number absent from PPT.

Metric	Current Qtr (Q2FY25)	YoY Change	QoQ Change	Trend	Mgmt Commentary
Volume (Total KT)	Not in document	↑ 15%	↓ (Mixed)	□	Non-energy volumes robust (+22% YoY); Energy volumes (MMA) crashed 34% QoQ.
MMA Volume (KT)	20.5 KT	First entry	↓ 33.9%	↓	Volume drop from 31 KT in Q1 due to gasoline-naphtha spread compression.
Utilization (%)	50-80% (Chain-wise)	First entry	First entry	→	NT (56%), Ethylation (48%), MMA (41%) - significant operating leverage available.
Revenue (□Cr)	□1,630 Cr (Implied)	↑ 12%*	↓ 12.3%	↓	H1 revenue □3,798 Cr; Q2 decline driven by Energy segment volume hit.
Gross Margin (%)	Not in document	First entry	First entry	□	Management notes pricing has "bottomed out" across most chemical chains.
EBITDA (□Cr)	□202 Cr	↓ 13.3%	↓ 35.0%	↓	H1 EBITDA □512 Cr (+18% YoY); Q2 hit by MMA spreads and China pricing.
EBITDA Margin %	12.4% (Implied)	↓ 360 bps	↓ 440 bps	↓	Compression due to lower Energy segment contribution and pricing pressure.
PAT (□Cr)	□52 Cr (Implied)	↓ 42.9%	↓ 62.1%	↓	H1 PAT □189 Cr vs □160 Cr YoY; Q2 includes □2.3 Cr exceptional gain.
ROCE (%)	< 10% (Est)	First entry	First entry	↓	Target >15% remains a multi-year goal (FY28).
Cash Flow (OCF)	Not in document	First entry	First entry	□	FCF negative due to H1 Capex of □670 Cr.
Net Debt / EBITDA	~3.3x	First entry	First entry	↓	Currently above comfort level of 2.5x; target to reduce by FY28.
R&D Spend (□Cr)	Not in document	First entry	First entry	□	Focused on asset-light growth and 5+ strategic alliance projects.
Working Capital	Not in document	First entry	First entry	↓	Extended cycles in textile industry/dyes impact intermediates.
**YoY Revenue change calculated from H1 trends.*					

2B. SEGMENT BREAKDOWN

Segment	Revenue Share (H1)	YoY Volume Growth	Margin Trend	vs Company Avg	Key Development
Agrochemicals	19%	Soft/ Recovering	↓ Pressure	Below Avg	Adverse weather in US/LATAM; recovery expected in H1CY25.
Dyes & Pigments	12%	↑ Robust	□Improving	Inline	Consolidation (Sudarshan/Heubach) to help domestic margins.
Energy & Additives	37%	↓ 36% (QoQ)	□Volatile	Above Avg	Hit by low gasoline-naphtha spreads; US bulk shipments started.
Pharmaceuticals	9%	↑ Steady	→ Stable	Inline	Biosecure Act tailwinds; pricing pressure in PAP (Paracetamol).
Polymers & Additives	13%	↑ Robust	□Improving	Above Avg	Contract #2 at peak volumes; trade barriers for China help AIL.

3. MANAGEMENT OUTLOOK & EXECUTION TRACKER

Dimension	Category	Management Target / Claim	Required Run-Rate / Mathematical Feasibility	Historical Delivery	Risk Flag
Guidance	FY25 EBITDA	□1000 - □1050 Cr	Needs □244-269 Cr/quarter in H2; Q2 was □202 Cr. (Moderate Risk)	Missed (Cut by ~40%)	High
Guidance	FY28 EBITDA	□1800 - □2200 Cr	Needs ~24% CAGR from FY25 base. (Stretch Target)	New Target	Medium
Guidance	Capex Plan	FY25: □1300-1500 Cr	□670 Cr spent in H1; □630-830 Cr to be spent in H2.	Revised Down	Low
Guidance	Capex FY26	~□1,000 Cr	Significant reduction to conserve cash.	N/A	Low
Balance	Debt / Leverage	Debt/EBITDA < 2.5x	Requires EBITDA to double by FY28.	Currently ~3.3x	High
Strategy	Cost Optimization	□150 - □200 Cr EBITDA	Savings from steam, power, and yield by FY28.	Ongoing	Low
Strategy	Asset Light Growth	Leverage R&D for tolling	No specific □target given.	Early Stage	Medium
Strategy	Return Ratios	ROCE > 15%	Requires significant margin expansion in Zone 4.	Historically Lower	High

4. ANALYST Q&A

Q#	Relevance (1–5)	Analyst / Firm	Theme Cluster	Category	Underlying Concern	Management Response & Investment Implication	Evaded / Not Addressed	Credibility (1–5)	Verdict
1	4.5	Surya Patra / PhillipCap	MMA Visibility	Business Overview	Scale and sustainability of the MMA business given it is 37% of revenue.	Management plans to scale from 2-3 refineries to 15-20 globally to mitigate individual client volatility. This cements MMA as the primary, albeit volatile, growth driver for the next 2 years.	Specific backward integration details.	4.0	Directional with evidence
2	4.0	Surya Patra / PhillipCap	FY25 Guidance	Financials	Guidance for FY25 (□1000-1050 Cr) seems conservative given H1 performance.	Management is guiding based on "higher degree of confidence" and seasonal US demand in Q4. This implies H2 must outperform Q2 by at least 25% per quarter.	None	3.5	Cautious & realistic
3	3.5	Aditya Khetan / SMIFS	Export Volume	Business Overview	Why are volumes declining while peers grow, and is MMA a 10-year story?	Management clarified freight costs were actually higher in Q2 and MMA is a "market development" story with no prior comparison. The long-term upside depends on "octane boosting" penetration.	Why peers are growing faster.	3.0	Vague on peer comparison
4	5.0	Rohan Gupta / Nuvama	Guidance Walk-back	Management Commentary	FY25 guidance cut by 40% vs expectations 6 months	Management admitted that assumptions on MMA ramp-up	None	2.5	Admitting over-optimism

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					ago; was it over-optimism?	speed and margin recovery in the core portfolio were too aggressive. This resets the trust baseline for management's forward-looking projections.			
5	4.0	Rohit Nagaraj / Centrum	Gasoline Spreads	Business Overview	Why are volumes down when gasoline consumption is up?	The product is linked to "octane premium" (gasoline-naphtha spread), not absolute gasoline volume. This confirms AIL's high sensitivity to specific refining deltas rather than general demand.	None	4.5	Clear on technicals
6	3.5	Abhijit Akella / Kotak	Capacity Ramp-up	Capex and Allocation	What held back NT and Ethylation volumes?	These are newly commissioned capacities; ramp-up is in progress but hit by the current weak pricing environment. Future growth relies on higher-end specialty products (Propylation) that peers don't offer.	None	4.0	Specific timeline
7	5.0	Archit / Barclays	Predictability & FCF	Financials	Predictability has	Volatility will be mitigated	Specific FCF	2.0	

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					vanished and FCF is negative for 3 years; what changes?	by diversifying the MMA customer base, and FY26 capex is being moderated to improve cash flows. Until FCF turns positive, the stock remains a "capital-heavy" risk.	positive date.		Deflected — key signal
8	3.0	Priyank Chheda / Vallum	Octane Market	Business Overview	Can AIL control the market development for MMA?	AIL is targeting a share of the 35 million-ton MTBE (octane booster) market, of which they are barely "scratching the surface." Market share gains depend on technical education of customers.	None	3.0	Vague but consistent
9	4.0	Ankur Periwal / Axis Cap	China Competition	Macro	Will China's lower pricing continue for 1-2 more years?	For commodity chains like PDA, yes; but for domestic-heavy chains like NCB/ Pharma, pressure should ease sooner. This suggests a bifurcated recovery path for the portfolio.	None	3.5	Directional

PATTERN FLAGS & SENTIMENT

- **MMA Volatility Anxiety:** Analysts are deeply concerned that MMA has introduced a "black box" volatility to Aarti's earnings. Management's defensive posture (calling it a "market development" story) suggests they are still learning the nuances of global refinery economics. This will remain a recurring friction point until quarterly volumes stabilize.

- **Guidance Credibility Crisis:** Multiple analysts (Gupta, Archit, Periwal) focused on the massive walk-back of FY25 targets. Management's tone was humble, effectively asking for a "reset" under the new CEO. Credibility will only be restored if H2FY25 hits the revised ₹500+ Cr EBITDA target.
- **FCF & Leverage Overhang:** The recurring question on "when will FCF turn positive" went largely unanswered with specific dates, though the cut in FY26 capex guidance is a reactive move to calm the street.

Analyst Sentiment Verdict: Analysts were **skeptical and demanding**. The 40% guidance cut created significant friction, and management was forced to admit to earlier over-optimism. Credibility has deteriorated, and the primary risk is now the "unpredictability" of the Energy segment.

GUIDANCE GAPS REVEALED IN Q&A

Topic	What Mgmt Claimed (Prior Q)	What Q&A Revealed	Gap / Walk-back	Risk to Thesis
FY25 EBITDA	~₹1,500 Cr (Implied)	₹1,000 - ₹1,050 Cr	40% Reduction	High - Earnings reset
MMA Ramp-up	Expected to be fast	Volatile & spread-linked	Slower "Market Development"	Medium - Timeline risk
Capex Plan	₹1,500 - ₹1,800 Cr	₹1,300 - ₹1,500 Cr	15% Reduction	Low - Cash conservation

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5. WHAT CHANGED vs PRIOR QUARTER

First entry — no prior quarter to compare.