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IPO Note – Indigo Paints Limited

18-January-2021

RETAIL RESEARCH

Issue Snapshot:
Issue Open: Jan 20 – Jan 22, 2021

Price Band: Rs. 1488 –1490 (Discount of Rs 148 for the eligible Employee)

*Issue Size: 7,853,423 eq shares
(Fresh Issue of 2,013,423 eq sh
+ Offer for sale of 5,840,000 eq sh)
Including Employee Reservation of 70,000 eq sh

Issue Size: Rs. 1168.6 – 1170.2 cr

Reservation for:

QIB	Upto	50% eq sh
Non Institutional	atleast	15% eq sh
Retail	atleast	35% eq sh

Face Value: Rs 10

Book value: Rs 49.20 (September 30, 2020)

Bid size: - 10 equity shares and in multiples thereof

100% Book built Issue

Capital Structure:

Pre Issue Equity:	Rs. 45.56 cr
Post issue Equity:	Rs. 47.57 cr*

Listing: BSE & NSE

Book Running Lead Manager: Kotak Mahindra Capital Company Limited, Edelweiss Financial Services Limited, ICICI Securities Limited

Registrar to issue: Link Intime India Private Limited

Shareholding Pattern

Shareholding Pattern	**Pre issue %**	**Post issue %**
Promoter & Promoter Group	60.1	54.0
Public & Non Promoter Non- Public	39.9	46.0
Total	100.0	100.0

*=assuming issue subscribed at higher band
Source for this Note: RHP

Background & Operations:

Indigo Paints Ltd (IPL) the fifth largest company in the Indian decorative paint industry in terms of revenue from operations for Fiscal 2020 and the fastest growing amongst the top five paint companies in India. It has achieved this position in a highly competitive Indian decorative paint industry on the back of multi-pronged approach. This includes introducing differentiated products to create a distinct market in the paint industry, building brand equity for primary consumer brand of "Indigo", creating an extensive distribution network across 27 states and seven union territories as of September 30, 2020, and installing tinting machines across its network of dealers. To create demand for differentiated products, it initially tapped into Tier 3, Tier 4 Cities, and Rural Areas, where brand penetration is easier and dealers have greater ability to influence customer purchase decisions. It subsequently leveraged this network to engage with dealers in Tier 1 and Tier 2 Cities and Metros as well.

IPL manufactures a complete range of decorative paints including emulsions, enamels, wood coatings, distempers, primers, putties and cement paints. It also identifies potential product needs from customers and introduces differentiated products to meet these requirements, and create a distinct market for its products. It is the first company to manufacture and introduce certain differentiated products in the decorative paint market in India, which includes Metallic Emulsions, Tile Coat Emulsions, Bright Ceiling Coat Emulsions, Floor Coat Emulsions, Dirtproof & Waterproof Exterior Laminate, Exterior and Interior Acrylic Laminate, and PU Super Gloss Enamel(together, "**Indigo Differentiated Products**"). Revenue generated, i.e. invoicing as per contracted price, from sales of Indigo Differentiated Products represented 26.68%, 27.58%, and 28.62% of its total revenue from operations in Fiscal 2018, 2019 and 2020, respectively. As the first company in India to develop these products, IPL has had an early mover advantage in the markets it is present in, which has allowed to realise relatively higher margins for these products compared to the rest of its product portfolio.

As of September 30, 2020, IPL owns and operates three manufacturing facilities located in Jodhpur (Rajasthan), Kochi (Kerala) and Pudukkottai (Tamil Nadu) with an aggregate estimated installed production capacity of 101,903 kilo litres per annum ("**KLPA**") for liquid paints and 93,118 metric tonnes per annum ("**MTPA**") for putties and powder paints. Its manufacturing facilities are strategically located in close proximity to raw material sources that reduces inward freight costs, lowering cost of raw materials. It also intends to expand its manufacturing capacities at its facility at Pudukkottai in Tamil Nadu, by adding capacities to manufacture water-based paints to cater to the growing demand for these paints. It works closely with its dealers and the painter community to understand customer preferences, receive feedback on products and that of its competition, which enables to formulate an effective strategy for product development, sales, marketing and pricing.

Objects of Issue:

The Issue comprises a Fresh Issue by IPL and an Offer for Sale by the Selling Shareholder.

Offer for Sale

The Selling Shareholders will be entitled to their respective portion of the proceeds of the Offer for Sale after deducting their proportion of Offer expenses and relevant taxes thereon. IPL will not receive any proceeds from the Offer for Sale and the proceeds received from the Offer for Sale will not form part of the Net Proceeds.

The Fresh Issue

IPL proposes to utilise the Net Proceeds towards funding of the following objects:

- Funding capital expenditure for expansion of the existing manufacturing facility at Pudukkottai, Tamil Nadu (the "Proposed Expansion") by setting-up an additional unit (the "Additional Unit") adjacent to the existing facility;
- Purchase of tinting machines and gyroshakers
- Repayment/prepayment of all or certain of IPL's borrowings; and
- General corporate purposes

Competitive Strengths

Track record of consistent growth in a fast growing industry with significant entry barriers: IPL is the fastest growing amongst the top five paint companies in India. It is the fifth largest company in the Indian decorative paint industry in terms of revenue from operations for Fiscal 2020. The Indian decorative paint industry presents significant entry barriers. These market entry barriers include the development of an extensive distribution network through relationships with dealers, the ability to set up tinting machines with dealers, as well as significant marketing costs and the establishment of a distinct brand to gain product acceptance. Differentiated, strategic approach in addressing these issues has resulted in continued success. IPL has achieved this position in a highly competitive Indian decorative paint industry on the back of multi-pronged approach. This includes introducing Indigo Differentiated Products to create a distinct market in the paint industry, building brand equity for its primary consumer brand of "Indigo", creating an extensive distribution network, and installing tinting machines across its network of dealers. The Indian decorative paints market is expected to record a growth rate of approximately 13% in value and 10.2% in volume through 2024, driven by an increase in the disposable income of individuals and families, and various housing schemes, among others.

Differentiated products leading to greater brand recognition and enabling expansion into a complete range of decorative paint products: IPL consistently seeks to launch first-to-market products by identifying niche product opportunities and introducing products that address these requirements. It was the first company to introduce certain category-creator products, including its Metallic Emulsions, Tile Coat Emulsions, Bright Ceiling Coat Emulsions and Floor Coat Emulsions in the decorative paint market in India. Other products that it introduced include Dirtproof & Waterproof Exterior Laminate, Exterior and Interior Acrylic Laminate and PU Super Gloss Enamel that comprise its value-added product portfolio. These category-creator and value-added products comprise its portfolio of Indigo Differentiated Products and are differentiated from other products based on their end-use specifications and in terms of certain added properties. As the first company in India to develop certain category-creator products, IPL has had an early mover advantage in the markets it is are present in, which has allowed it to set the pricing terms for these products (*Source: F&S Report*), resulting in higher margins for these products compared to the rest of its product portfolio. Owing to the distinct market they cater to, and as only few other companies continue to manufacture these products it focused its marketing efforts on this portfolio, resulting in increased acceptance and demand, thereby enhancing brand recognition for these products across network of dealers. These products have enabled to build strong brand equity among end-customers and dealers thus aiding penetration of other decorative paint products.

Focused brand-building initiatives to gradually build brand equity: IPL has strategically undertaken brand-building initiatives to gain visibility with prudent use of resources, gradually increasing branding and marketing expenses consistent with the growth of its business. Its advertisement and sales promotion expenses represented 11.22%, 12.63%, and 12.65% of its revenue from operations in Fiscal 2018, 2019 and 2020, respectively. Its Media Advertising Spends (that are a part of advertising and sales promotion expenses) has gradually increased over the years, and amounted to Rs. 615.15 million in Fiscal 2020. Its media advertising spend in Fiscal 2020 is comparable to the spend incurred by the major companies (excluding the market leader). IPL's concentrated brand building efforts has helped develop brand equity with limited spend over the years in a market that has historically been dominated by companies that has invested considerable resources on developing their brand over several decades. It has strategically branded its products under the distinct and primary consumer brand of "*Indigo*" with different labels based on price points such as "*Platinum Series*", "*Gold Series*", "*Silver Series*", and "*Bronze Series*" rather than focusing on product-specific sub-brands. It has leveraged its brand recognition and goodwill in the market for its Indigo Differentiated Products, by gradually introducing and gaining visibility for its other product segments. This approach has allowed IPL to efficiently manage marketing and advertisement expenses and yet achieve extensive brand recognition within a relatively short period of time.

Extensive distribution network for better brand penetration: Paint companies are required to spend significant resources to develop their distribution network to increase the visibility and reach of their products through direct distribution to dealers. The dealers are typically multi-brand and are located across Metros, large cities, towns as well as Rural Areas. For a paint company, the market knowledge, financial resources and time required to develop such a network is significant. It has established its distribution network gradually and strategically through the bottom-up approach with prudent use of time, cost and resources. As a relatively new entrant in the market, IPL first focused on dealers in Tier 3, Tier 4 Cities, and Rural Areas, where brand penetration is easier and dealers have greater ability to influence customer purchase decisions. This helped IPL engage with a larger base of dealers across Tier 3, Tier 4 Cities, and Rural Areas, which it subsequently leveraged to expand into larger cities and metros. Its dealer network is also well integrated with its marketing and promotional activities, and helps in strengthening brand image. It has a well-integrated SAP system to manage inventory and effectively service its dealers. For efficient service, it engages with dealers through depots that it has set-up at major locations across distribution network. As of March 31, 2018, 2019, 2020 and as of September 30, 2020, IPL had 33, 33, 36 and 40 depots, respectively.

Leveraged brand equity and distribution network to populate tinting machines: Emulsions are the largest and among the fastest growing product segment within the Indian decorative paint industry. The market for emulsions was valued at Rs. 163.9 billion in Fiscal 2019, and is expected to grow at a CAGR of 13.60% and amount to Rs. 309.5 billion by Fiscal 2024. Different shades of emulsion paints are produced through in-shop tinting machines present at dealer outlets. These tinting machines are unique to each paint manufacturer due to design specifications including with respect to colorants, emulsion bases, fan-decks or shade cards, and customized software applications. IPL has, through its focused branding efforts, been able to gain recognition within the Tier 3, Tier 4 Cities, and Rural Areas that it caters to, where the existing population of tinting machines is relatively low. This has introduced it to a large number of dealers that have few or no tinting machines at their premises, thereby making acceptance of its tinting machines at these locations relatively easier. IPL is now gradually adding tinting machines at dealer outlets in larger cities and Metros as well.

It started installing tinting machines in Fiscal 2014, which gained momentum from Fiscal 2018. During the last three fiscals, IPL installed an average of 1,223 tinting machines every fiscal, and as of September 30, 2020, it had a total of 4,603 tinting machines across its network of dealers in India. Its tinting machines are manufactured by recognized international companies and are capable of producing unlimited shades. While it actively promotes its machines, increasing acceptance of its machines by dealers indicates greater demand for its emulsion products and stronger commitments by dealers to continue their engagements with the Company.

Strategically located manufacturing facilities with proximity to raw materials: As of September 30, 2020, IPL operated three manufacturing facilities in India, located in the states of Rajasthan, Kerala and Tamil Nadu. It plans its capital expenditure in advance and has periodically carried out capacity expansions at its facilities to cater to the increased demand for its products. Its manufacturing facilities are strategically located in proximity to its raw material sources, which reduces inward freight costs and results in lower cost of raw materials.

IPL strengthened its presence in southern India and gained access to solvent-based paints through the acquisition of Hi-Build Coatings Private Limited and its facilities at Kochi (Kerala) and Pudukkottai (Tamil Nadu) in Fiscal 2016. For water-based paints manufactured at Kochi (Kerala), the principal raw materials are acrylic emulsions that it predominantly source from the neighboring states of Tamil Nadu and Karnataka, minerals that it principally import from Vietnam, and titanium dioxide and china clay that are available within Kerala. For solvent-based paints manufactured at Pudukkottai (Tamil Nadu), the principal raw materials include alkyd resins that it mainly source from manufacturers based in Tamil Nadu and the neighboring state of Telangana, and turpentine oil that is available from refineries within Tamil Nadu. As a result of locational advantages and the higher margins generated from the Indigo Differentiated Products, IPL's Gross Margins have consistently been higher than the industry average.

Well-qualified and professional management team with a committed employee base: IPL has a strong management team with considerable industry experience. It also has a well-qualified senior management team with extensive experience in the paint industry, which positions it well to capitalize on future growth opportunities. The heads of functional groups, such as production, finance, strategy and planning, enhance the quality of its management with their specific and extensive industry experience. IPL is supported by its committed employee base and has a mutually beneficial relationship with its employees. It also incentivize its employee base through ESOPs and performance-linked incentives, that has helped contain employee attrition.

Business Strategy:

Continue to focus on developing differentiated products to grow market share: IPL intends to continue to grow its portfolio of differentiated products going forward as these products have widened the end-user base that it caters to and typically have a higher margin profile than other decorative paint products. In particular, it will continue to identify potential product opportunities in the market, and focus on developing category-creator products to cater to distinct requirements in the Indian decorative paint industry. It also seek to innovate and develop products with distinguished properties by undertaking research, attending industry trade fairs, and keeping abreast with industry trends and practices. By introducing more category-creator and value-added products, it expects to continue to benefit from the early mover advantages that it has experienced in the past. IPL will continue to leverage the brand equity and dealer network created by these niche products to distribute its wide range of products in markets where it has been present for a considerable period, and to enter new markets, to further increase its market share.

Further strengthen brand to consolidate position as a leading paint company in India*:* IPL has been making consistent efforts to strengthen the "Indigo" brand and increase brand recall through marketing initiatives. It has consciously developed its portfolio of products under the primary consumer brand of "Indigo", with variants such as "Platinum Series", "Gold Series", "Silver Series", and "Bronze Series", for better brand recall. It has also standardized its packaging design to provide uniformity and enable easier brand recognition at dealer outlets. IPL's advertising efforts have been focused on select products that differentiate it from its competitors. IPL has over the past three fiscals gradually increased its media advertising spends consistent with financial growth. Having attained near parity with the large players in terms of absolute media advertising spend in Fiscal 2020 (Source: F&S Report), it now intends to make only marginal increases in its future media advertising expenses, and leverage its current cost structure to achieve growth and drive profitability while strengthening its brand. IPL intends to increase the visibility of its products in larger cities within states where it already have a presence in Tier 3, Tier 4 Cities, and Rural Areas. It also proposes to leverage the goodwill it has generated with its Indigo Differentiated Products, to expand branding efforts to its overall product portfolio.

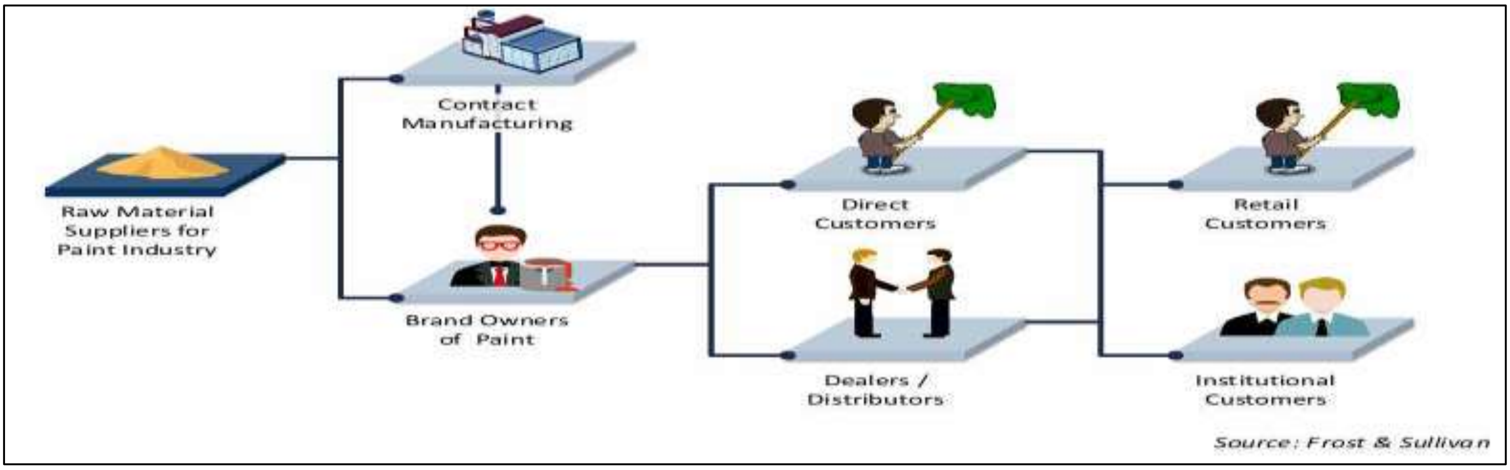
Deepen penetration in existing markets and expand presence in select new territories by populating tinting machines: IPL's key focus is to increase its penetration in the markets where it currently operates by replicating the same proposition that has helped it grow in the past. There is significant untapped opportunity in Metros and larger that can be capitalized by expanding distribution network. In states where IPL has been present for a significant period of time such as Kerala, West Bengal, Bihar, Jharkhand, Chhattisgarh, Odisha and Uttar Pradesh, it has expanded its existing network in Tier 3, Tier 4 Cities, and Rural Areas, outwards into Tier 1 and Tier 2 Cities. In states that it has recently entered such as Telangana, Gujarat, Maharashtra, Karnataka and Tamil Nadu, it intends to similarly proliferate its presence in these regions by first targeting Tier 3, Tier 4 Cities, and Rural Areas, and then leveraging this network to larger cities, to be able to capture and build on the dealer network in these regions. As of March 31, 2020, IPL had a network of 3,292 Active Dealers in these five states, and intends to engage with more dealers to strengthen its existing sales infrastructure and network in these regions. IPL also is in process of increasing presence in North India, particularly in the states of Punjab and Uttarakhand, and the union territory of Jammu & Kashmir, where it has recently commenced distributing its products.

In markets where IPL is not present, it intends to initially market and distribute its portfolio of Indigo Differentiated Products followed by entire portfolio of products. In order to increase distribution and sale of its emulsion products, IPL continue to invest in populating tinting machines. It has been gradually leveraging its growing brand equity and adopting alternate means to provide tinting machines with inbuilt computers to achieve this.

Expand manufacturing capacities*:* IPL intends to expand its manufacturing capacities to aid growth efforts and consolidate its pan-India presence. To cater to the increased demand for water-based paints, it intends to use a part of the Net Proceeds towards expansion of its manufacturing facilities. IPL currently manufactures only solvent-based paints at its manufacturing facility in Tamil Nadu. It intends to expand its capacities at Pudukkottai, Tamil Nadu, to include manufacturing of water-based paints to cater to the growing demand for water-based paints. In order to achieve this, it has acquired additional land adjacent to its existing unit at Pudukkottai, Tamil Nadu and has finalized the blueprint and design specifications for the first phase of the proposed expansion. IPL is also in the process of carrying out capacity expansion plans at its existing Jodhpur Facility. These additions are being carried out at both Unit I and Unit II with respect to liquid paints such as emulsions and primers, and powder paints such as putties.

Industry

Indian Paint Industry



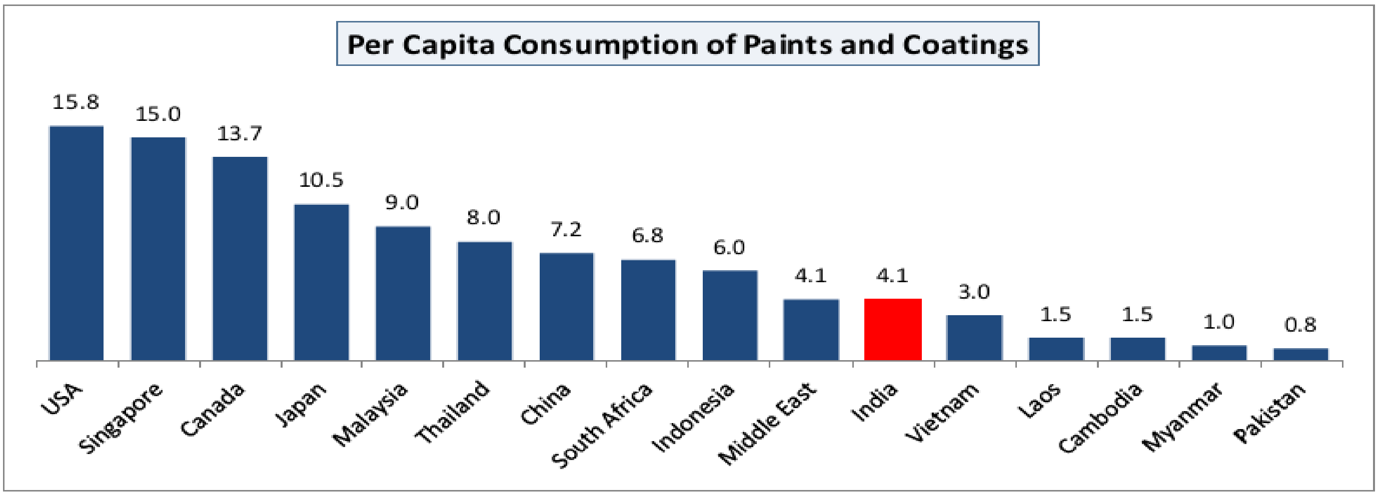
The industry has a three-stage setup comprising raw material suppliers, manufacturers and sellers. Most of the raw materials in the paint industry are petroleum based, supplied by petrochemical companies. A few companies adopt contract manufacturing, while bigger companies have their own manufacturing facilities. The larger chemical companies are vertically integrated in both the raw materials and paint production stages while others are pure-play producers of paint and coatings. For example, Asian Paints and Berger Paints produce their own emulsions that are used in the production of paints. Most sales are driven through dealer and distributor networks, which sell onwards to local buyers. Hardware stores are usually the retailers in the paint and coating industry, while the other major retailers may have paint and coating segments within their broad range of offerings. Direct sales are a minor component of overall sales. The Indian decorative paint industry has significant entry barriers. These market entry barriers include the development of an extensive distribution network through long-term relationships with dealers, the ability to set up tinting machines with dealers, as well as significant marketing costs and the establishment of a distinct brand to gain product acceptance.

Raw Material Analysis

Raw material sourcing comprises more than 60% of the input costs of paint manufacturing. Around 300 to 400 ingredients are used in the manufacturing of decorative paints, of which, Titanium Dioxide (TiO_2), a white pigment, constitutes around 20% to 25%. The paint industry has historically been successful in passing on any significant price increases in inputs to the customers. TiO_2 is derived from ilmenite, and while India has significant ilmenite reserves, there is a limited market for its products and derivatives, particularly TiO_2, in India. However, companies failed to expand their capacity for TiO_2 resulting in end-users relying on imports. As a result, the Indian paint industry has been importing TiO_2 from China despite it being available in India. Kerala Metals and Minerals is one of the leading manufacturers of TiO_2 in India. For water-based paints, the principal raw materials are acrylic emulsions and compounds such as TiO_2, china clay and certain minerals. While Asian Paints, Berger Paints and Kansai Nerolac make their emulsions in-house by importing raw materials such as monomers, Indigo

Paints procures it locally as purchasing emulsion instead of producing it has a cost benefit thereby providing higher margins. Apart from TiO2, the other raw materials being used for water based paints and putty are white cement, minerals including lime, dolomite, calcite and talcum. As on 2015 as per NMI data, the total reserves of dolomite in India was around 8,415 MMT and Rajasthan is estimated to have approximately 590MMT resources of dolomite. The total reserves of calcite have been estimated at about 23 MMT, with Rajasthan having the largest share (53%) of calcite resources. The total reserves of talc, another major raw material, have been estimated at 316 MMT. Substantial quantities of reserves are established in Rajasthan (57%). Limestone is also one of the key raw materials for manufacturing of paints. In the Fiscal 2018, there were 680 reporting mines together producing 379 MMT of lime. Rajasthan was the leading producer accounting for (20%) of the total production of limestone. Indigo Paints has strategically located its manufacturing facilities close to the source of the raw material for ease of procurement and to reduce delivery and logistical costs.

India Per Capita Paint Consumption



Source: Bloomberg, Frost & Sullivan

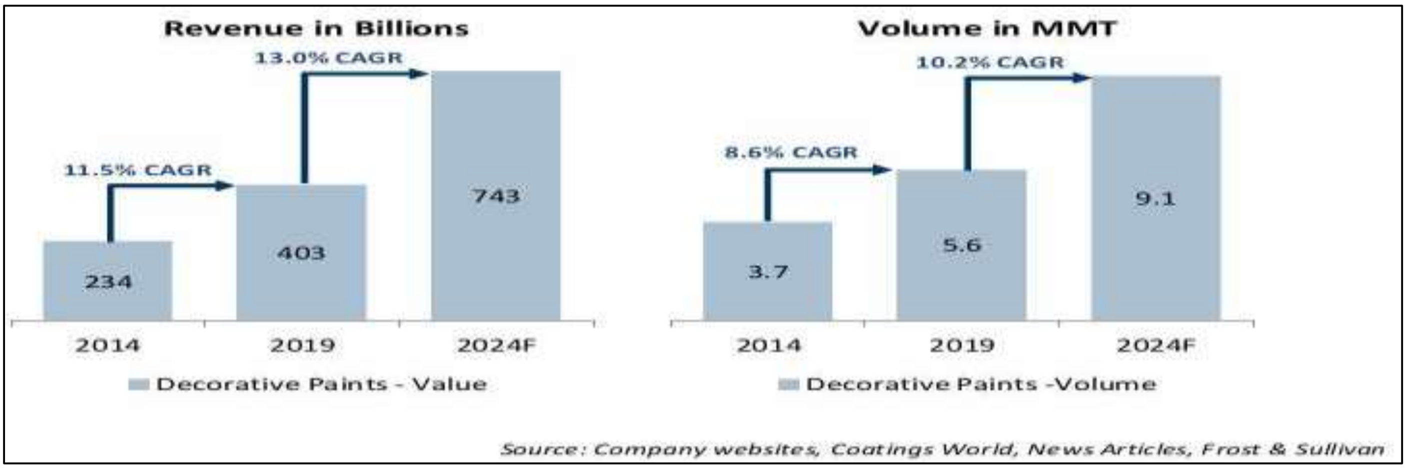
The average consumption of paints and coatings for Asia Pacific is 4.7 kg while that of the developed nations in Asia Pacific have an average consumption of 9.7 kg.

India's per capita paint consumption increased by a CAGR of 6.8% in the last seven years from 2.6 kg in Fiscal 2012 to 4.1 kg in Fiscal 2019. Compared to the global average consumption of approximately 14 kg to 15 kg per capita, the per capita consumption of paints and coatings in India is low, indicating a significant opportunity for market penetration in India.
The industrial sector aided by impetus in infrastructure, is expected to drive the GDP growth, resulting in increased consumption of coatings. The increasing GDP per capita and a growing middle class population are expected to raise the per capita paint consumption by 30% to 40% during Fiscal 2020 to Fiscal 2022. Increasing urbanization coupled with rise in disposable income is leading to an increased spend on decorative paints.

The Indian paint industry comprises a sizeable portion of India’s GDP. The industry has registered a CAGR of approximately 11% during Fiscal 2014 to Fiscal 2019, almost double the growth rate of India’s GDP. The high growth
The decorative paint segment constitutes around 74% of the total paint sales, resulting in the paint sector growing at a robust rate even at the time of an industrial slowdown. The Indian paint industry is valued at approximately Rs. 545 billion and is expected to grow to amount to Rs. 971 billion by 2024. There is a strong co-relation between the Indian paint industry and the GDP growth of India. It has historically almost doubled India's GDP growth rate. Going forward, the decorative paint market is expected to grow at a CAGR of 13% while the industrial paint market is expected to grow at a CAGR of 9.9% by 2024.

The consumption of water-based paints is rising globally, and the demand is expected to remain high as Indian paint manufactures are shifting from solvent-based to water-based paints. Around 55% of the raw materials used by the paint companies are crude oil derivatives and comprise approximately 30% to 35% of the sector's overall raw material costs. The prices of crude oil and its derivatives are volatile and fluctuate, exerting pressure on the prices of paints. The prices have been fluctuating on the lower end since 2018 with 2020 experiencing the lowest prices. The oil and gas industry has experienced a price collapse for the third time in the last decade; 2020 price collapse being a combination of supply shock and an unprecedented demand drop. The overall fluctuating prices of oil are creating a major pricing issue for paint companies. The recent capacity increases announced by key paint firms is also focused on water-based systems.

Decorative Paints
Set forth below is the market size of the Indian decorative paints market, in value (Rs. billion) and in volume (MMT), for 2014, 2019 and 2024 (forecast):



The decorative paints segment represents around 74% of the overall paint market in India and includes wall finishes for interior and exterior use, enamels, wood finishes and ancillary products such as primers and putties. Over the past five years, the share of decorative paints has increased from 67% to 74% (Fiscal 2019).

The decorative segment has grown at a CAGR of 11.5% from Fiscal 2014 to Fiscal 2019, driven by the increase in consumption of paints in Tier 2 – 4 Cities. COVID-19 has impacted the metro cities and Tier 1 Cities more with most regions being under complete lockdown. As a result, the industrial recovery outside the main cities has been faster. For the paint industry, Rural Areas and Tier 2 – 4 Cities account for nearly half the total sales. Accordingly, the pandemic-led decline in demand is likely to have the least impact on Indigo Paints as compared to the other players as it predominantly operates in Tier 2 – 4 Cities.

The decorative paint industry appears to be shifting from 'digitization' to 'digitalization' with the installation of bots, use of state-of-the-art tools for planning and distribution and use of nanotechnology. The growth and deployment of tinting machines at all dealer counters enables customers to select their desired shade. Colour combinations are also offered to the customers as a virtual visualization of their homes before physically painting their homes.

The Indian decorative paints market is expected to growth at a CAGR of approximately 13% in terms of value and 10.2% in terms of volume through 2024 driven by a number of factors including increase in the disposable income of individuals and families and various housing schemes. The Government schemes and policies like 'Housing for All' will also be a major driver for growth of fresh painting. With more such initiatives targeted for the regional population, the demand from smaller cities and towns is estimated to grow faster benefitting companies like Indigo Paints, which already has an established presence in these geographies.

Set forth below is the growth (CAGR) recorded by the Indian decorative paints industry, segmented based on sub-product type, in terms of value (Rs. billion), from 2014 – 2019, and forecast for 2019 – 2024:

	Enamels	Emulsions	Primers	Distempers	Wood Coatings	Putties	Others
2014-19	13.6%	11.4%	11.8%	9.9%	8.6%	10.0%	8.4%
2019-24F	14.2%	13.6%	12.3%	10.9%	9.6%	11.7%	11.0%

Source: Coatings World, News Articles, Frost & Sullivan

Within the decorative paint market, enamels and emulsion paints are the fastest growing segments. Emulsions are the largest segment with increasing popularity among the masses as they are less toxic than most oil-based paints, release less number of VOCs and are devoid of any strong odor. Increasing penetration of emulsions is driven by the varying degrees of shine that manufacturers offer in these paints. The market for emulsions was valued at Rs. 163.9 billion in Fiscal 2019, and is expected to grow at a CAGR of 13.6% and amount to Rs. 309.5 billion by Fiscal 2024.

There has been a higher growth of emulsion paints for interiors as compared to distempers, in line with an increase in the use of economy emulsions in place of lower-priced distempers. Even in the exterior category, emulsion-based coatings are being preferred against the conventional cement-based coatings. Seeking better products, consumers are also switching to marginally higher-priced emulsions with more durability and better-looking finishes in a wider range of colors.

The Indian decorative paint industry has been witnessing a gradual shift in preferences from the traditional whitewash to high-quality paints like emulsions and enamel paints, providing stable base for growth of Indian paint industry. In addition, it is creating a strong competitive market, where players are adopting different strategies to tap the growing demand in the market for a larger share. Further, increased focus on education, urbanization, development of the rural market, and introduction of many innovative products such as odor free, and dust and water-resistant paints, are major drivers that are propelling the growth of the paint market in India. The decorative paints industry is expected to grow at a CAGR of 13% through 2024 with enamels and emulsions expected to record a CAGR of 14.2% and 13.6% respectively.

In the past few years, the industry has witnessed a gradual shift in consumer's preference from the traditional whitewash to better quality, 'value for money (VFM)'/'bottom of pyramid (BOP)' paint, especially in Tier 2 – 4 Cities. The demand for putty, distemper, lower-end enamels, among others, is expected to grow in the coming years.

Other products that are expected to grow in performance are low-value products such as putty and distempers. The reduction in the goods and services tax (GST) on paints, varnishes and putty, from 28% to 18% in July 2018, has driven growth in these segments. The direct application of paints on cemented or plastered walls is now reducing as rural consumers are becoming aware of the benefits of applying putty over walls prior to painting. Demand for putty is also being driven by incentivizing painters to purchase putty along with paints. However, this trend is not expected to continue going forward and the current surge in demand for distemper and putty is expected to normalize with an increase in consumption of enamel and emulsion paints.

Indian Decorative Paint Market – Trends

GST rate reduction boosting the sector. The GST rate for paints has reduced form 28% to 18% spurring volumes in the decorative market, particularly in the lower-end segments like emulsions, distempers and putty. Paint firms have passed the cost benefits on to the customers creating a positive demand for paints owing to lower prices.

Portfolio diversification. Most companies are now venturing into new product segments and focusing on diversifying their product portfolio. Many paint companies entered the segment for waterproofing and building chemicals in the last few years. While there has been a substantial change in focus towards waterproofing over the last decade, this was previously considered as an extra expense in the Indian market.

Movement towards decorative paints over conventional whitewash. The segment has been driven by urbanization, the shortening of the re-painting cycle and industry initiatives such as expanding reach and introducing a variety of decorative products. The industry has recently witnessed a gradual shift in consumer preference from traditional whitewash to better, value for quality and value for money (VFM)' /'pyramid bottom (BOP)' paint, especially in the Tier 2 – 4 Cities.

Focus on growing bottom of the pyramid space. The industry's leading players have focused on increasing the bottom of the pyramid space, which is much broader in terms of volume as compared to the top and mid-segments. Further, companies reiterated that while the premium ranges continue to grow, the economy range (including emulsion, distemper and putty) have been widening at a higher rate, i.e. increased awareness among rural households to apply undercoat (putty and primer) before applying the paint (distempers) has helped drive demand of low-end products as well.

Initiatives by companies. Most of the eminent players in the decorative paint segment have attempted to actively expand their distribution network to penetrate the Indian market. Due to the rising number of smaller towns and villages, the strength of dealers, which has been projected at 120,000 to 150,000 outlets, is expected to grow at a CAGR of approximately 10% annually. Owing to this growth rate, companies have proactively expanded their distributor base in newer geographies, especially in Tier 2 – 4 Cities and Rural Areas. Indigo Paints initially tapped into the unsaturated markets of the Tier 2 – 4 Cities, where brand penetration was easier and the dealers had a greater ability to influence the customers' purchase decisions. These Tier 2 – 4 markets provided significant opportunity for growth and helped the company multiply its revenue and considerably expand its brand and presence in the Indian market.

Sustainable products and shift towards low VOC content. The paint companies have introduced products that provide health-centric services, such as anti-bacterial and anti-pollution/ air-purifying, and anti-fungal and stain resistant products. The market perceptions of the adverse effects of VOCs combined with stringent environmental legislations have increased the demand for low/ zero VOC paints and coatings. In India, the regulatory changes are driving the increase in adoption of water-solvent and high-solid coatings which have lower VOC content. Moreover, the adoption of green technologies and bio-based materials has seen to positively impact water-based coatings demand in the country.

A diversified customer base with under penetration, lower competitive intensity and stifled demand has brought the growth of the paint industry almost in line with the traditional fast-moving consumer goods industry, making it an appealing investment for a long-term investor. The competitive and economic demand will remain critical considerations for further market penetration.

Growth Drivers

Government's 'Housing for All/ affordable housing' measures has helped fresh demand for painting and will help re-painting demand in the future. Pradhan Mantri Awas Yojana (PMAY), an initiative by the Government of India ensures affordable house for all in the urban areas with a target of building 20 million affordable houses by March 31, 2022. It has two components: one for the urban poor and the other for the rural poor. Under the urban component, a demand of 11.2 million houses in urban areas has been validated. In Fiscal 2020, the total number of houses sanctioned under the scheme had crossed 10 million.

- Smart cities - In order to sustain the rapid urbanization in India, the Government launched the Smart City Mission in 2015, with an intention to develop 109 cities as Smart Cities over the next 5 years. This is expected to lead to larger number of commercial and residential complexes being created driving the demand for decorative paints.

- AMRUT - Atal Mission for Rejuvenation and Urban Transformation was launched by the Government to provide basic civic amenities which will involve renovation of 500 cities.

- Urbanization – The rise in urbanization, supported by demand for real estate and improved infrastructure, has increased the application of paint. India's trajectory of urbanization has grown well from 25.6%in 1990 to 34.5%in 2019 (34.9% in 2020 (estimated). The rise in urbanization, supported by demand for real estate and improved infrastructure, has increased paint application. The UN expects that by 2030 approximately 40% of the population of India will reside in urban areas. Urban areas contributed 47.0% of India's GDP in 2000, and are expected to contribute to 70.0% of India's GDP in 2030.

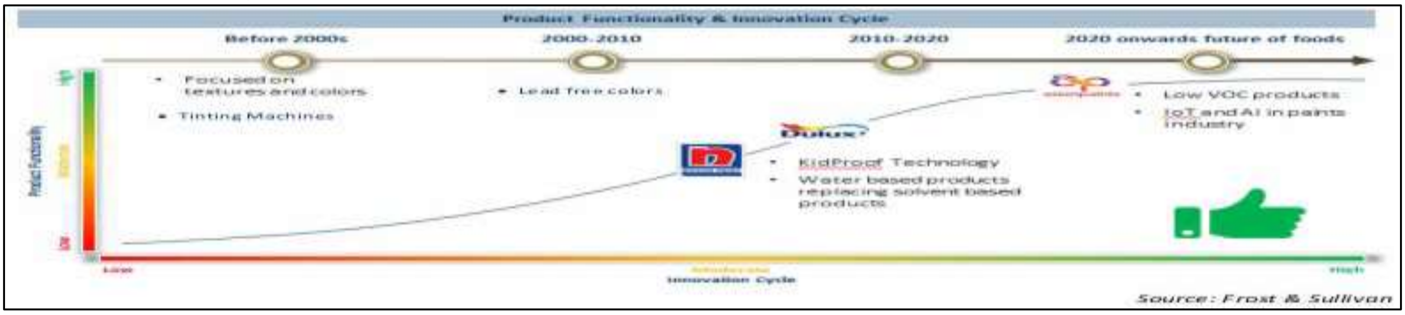
- Real Estate Sector Growth – The residential real estate sector (top 7 cities) has remained resilient in 2019 with sales increasing 6% year-on-year despite muted consumption expenditure. However, there have been challenges in 2020 in India owing to the impact of the on-going pandemic. The first quarter of Fiscal 2020 witnessed a decline in sales on a year-on-year basis as the buyers deferred their purchase decisions due to the impending crisis, which led to the sales declining by nearly 30% in the first quarter of Fiscal 2020 on a year-on-year basis. The real estate sector in India is expected to reach US$ 1 trillion by 2030. By 2025, it has been estimated to contribute 13% to India's GDP. Emergence of nuclear families, rapid urbanization and rising household income are likely to remain the key drivers for growth of real estate.

Innovations in the Industry

The industry has witnessed shifts in upgrading/ pre-minimization over more than a decade, including moving from: (i) distemper to nterior emulsion; (ii) mid-segment to top-end segment; (iii) low-end to top-end segment; (iv) cement paint to exterior emulsions; and (v) unorganized to organized in smaller towns, especially in Tier 3 and 4 Cities and Rural Areas.

While metros and Tier 1 and 2 Cities comparatively contribute significantly to the top-end product market, smaller towns have also indicated increased interest in premium products, on the back of increased consciousness of aesthetics and availability of resources to opt for better quality products at higher prices. Another reason for opting premium variants is inflexible labour cost at all levels, making option of paint variant relatively indifferent. There have currently been fewer options available in the value-added sub category and mainly in the premium price ranges. However, with an increasing demand for these products, the companies are likely to launch more specialized products.

Set forth below is the product innovation cycle in the Indian paints industry:



Tinting Machines increasing Barriers to Entry

Tinting machines have created hindrances to the delivery network. Many dealers are unable to install a new company's tinting machine mainly due to space constraints. The large number of SKUs and product ranges in emulsions renders installation of tinting machines imperative for timely distribution of different shades and products.

Installing tinting machines has been crucial in improving reach and enabling dealers to meet customer requirements, thereby reducing the expense of inventories. In order to match colours that suit the evolving needs of consumers, paint companies must have a range of colours that suit the consumer requirements and needs. Tinting machines come with added benefits of consistency, advanced technology, precision, high dosing speed and ease of operation. In the paint store, the tinting system provides the end user with a full solution compliant with the coating industry standards. By building a large network of more than 70,000 dealers, Asian Paints has developed its distribution network in a unique way. Since these dealers have low working space to store a wide range of paints, the business has built on tinting machines with the dealers retaining a maximum of one or two tinting machines to support the customers.

Different shades of emulsion paints are produced through in-shop tinting machines present at dealer outlets. These tinting machines are unique to each paint manufacturer due to the design specifications with respect to colorants, emulsion bases, fan–decks or shade cards, and customized software applications. These tinting machines are a pre-requisite for all dealers who sell emulsion paints. However, a stiff resistance for installation of these machines is encountered from dealers due to lack of physical space at their counters. As a result, most dealers tend to install tinting machines of only recognized players. Indigo Paints has installed tinting machines across India through their focus on branding efforts, specifically in Tier 2 – 4 Cities and Rural Areas where the penetration of tinting machines is relatively low.

Digital Marketing
The ability of retail customers to visualize the colour of an architectural coating has been the key focus of digital marketing initiatives. Almost all leading manufacturers of architectural coatings now have a strong colour visualizer strategy to maintain their market share. However, there are other aspects of digital marketing as well including a digital magazine issued by Asian Paints, and digital communication channels developed by Kansai Paints by collaborating with construction companies.

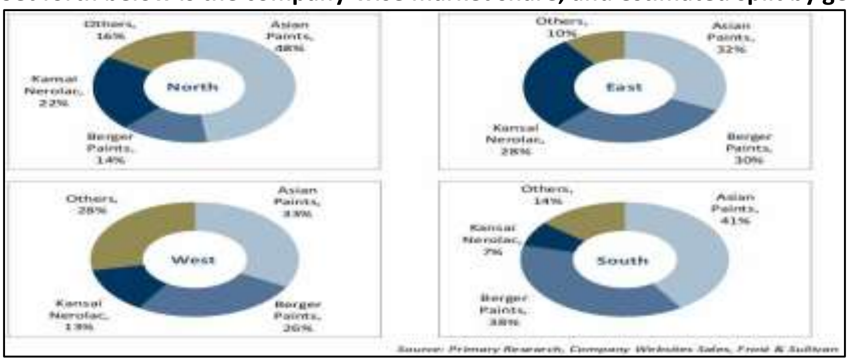
Nanotechnology in paints
Nanomaterial is applied to improve paint's efficiency and provide it with new functionalities. For example, paints are easy to clean and are water/ dirt repellent, UV-protected, antimicrobial resistant, scratch resistant, with increased longevity.
Indigo Paints has been able to establish itself with a strong brand recall and a significant first mover advantage in product innovation. With Indigo Paints trying to expand its geographical reach and dealer network, a focus and investment on the use of technology across operations will benefit it further. Digitalization will help Indigo Paints adapt to the changes in the current market trends and anticipate the future trends as well.

India Decorative Paints Industry: Market Share Analysis
Oligopolistic market with strong entry barriers led by brands and distribution
The Indian paints and coatings market has been consolidated unlike the markets in Russia and China. The organized sector comprises major players such as Asian Paints, Kansai Nerolac, AkzoNobel and Berger Paints lead the business. The Indian paints market has been dominated by the decorative market contributing approximately 74% of the total paints market. The top 10 to 12 players account for around 77% of the organized market within the decorative market. The remaining 23% comprises small players.

Asian Paints is the market leader in the decorative paints industry and accounts for 42% of the total market. The decorative paint segment accounts for 95% to 97% of Asian Paints' revenue. Berger Paints follows Asian Paints in the decorative category to become the second largest contributor in the market, followed by Kansai Nerolac with over 45% to 50% of its revenue being derived from industrial paints. Akzo Nobel has slowly expanded its reach in the decorative market by evaluating options in the smaller cities with lesser competition.

Indigo Paints started its operations in 2000 and has been present across segments such as interior and exterior emulsions, enamels, wood coatings, putty, primers and ceiling and floor coats. Being the fifth largest player in the decorative segment, it has recently entered bigger markets such as Mumbai and Delhi. Other small paint companies with sizeable presence include Shalimar Paints, Nippon Paint India, Kamdhenu Paints and JSW Paints. Paint companies with lesser presence include Jenson & Nicholson Paints Private Limited (JNPL), Snowcem Paints, and Jotun Paints.

Set forth below is the company-wise market share, and estimated split by geography:



While most parts of India are largely dominated by Asian Paints, Asian Paints has a larger presence in Metro and Tier 1 Cities of these regions. The newer players such as JSW are establishing their presence in the southern region. The western regions, Maharashtra in particular, has seen a significant involvement of smaller players driven by the demand mainly from Tier 2 – 4 Cities. The competition has increased with the introduction of JSW Paints and Indigo Paints in the industry. The regional players such as Kamdhenu Paints have become aggressive to capture expand their position and gain more market share. Unlike the bigger players, Indigo Paints entered the market consisting of small cities, towns and Rural Areas. While the bigger paint companies are now tapping the Tier 2 – 4 Cities, Indigo Paints is leveraging its brand in those markets by venturing into Metros and Tier 1 Cities.

Market Penetration

Paint companies are required to spend significant resources to develop their distribution network to increase the visibility and reach of their products through direct distribution to dealers. The dealers are typically multi-brand and are located across metros, large cities, towns and Rural Areas. The market knowledge, financial resources and time taken to develop such a network is significant.

Product Portfolio

The industry has witnessed shifts in paint up-gradation in the last few years, the shift has mainly been from: (i) distemper to interior emulsion; (ii) mid to top-end category; (iii) bottom to top section; (iv) cement paint to exterior emulsions; and (v) unorganized to organized in smaller towns, especially in Tier 3 – 4 Cities and Rural Areas.

While metro, Tier 1 and to some extent Tier 2 Cities, have a relatively greater contribution to the top-end product offering, the demand and interest for premium products has been witnessed from the smaller towns as well. The customers are now more aesthetically conscious even in Rural Areas and have the means to opt for better quality products.

The advertising and branding strategy of Indigo Paint has been the differentiating factor. Indigo Paints operates only under one brand name, "*Indigo*". This strategy has helped the customers connect to the brand immediately without having to remember multiple brand names. Indigo Paints differentiates its products on the basis of the price point as Platinum, Gold, Silver and Bronze series. Indigo Paints has managed to keep its packaging uniform across all its brands to enhance brand recognition. Another characteristic that differentiates Indigo Paints' advertising strategy is that it only advertises its differentiated products. Indigo Paints was the first among its competitors to introduce coatings for the ceiling, tile and floor, with the competitors entering this space only now.

Indigo Paints is well established in Tier 3 and 4 Cities with extremely high penetration. Indigo Paints' media advertising spend has gradually increased over the years, and was comparable to the spend incurred by the major entities (excluding Asian Paints), in Fiscal 2020.

Indigo Paints has effectively managed to establish itself as a differentiator in the existing product categories in addition to evolving as a category creator by bringing new product innovations to the market. The company first introduced Metallic Emulsions in 2005 and has since entered new markets by introducing other differentiated products with regularity. Most recently they introduced their Exterior and Interior Acrylic Laminate and Enamels such as the PU Super Gloss Enamel in 2016, Dirtproof & Waterproof Exterior Laminate in 2017, resulting in a portfolio of seven such differentiated products as of September 30, 2020.

Owing to the distinct market they cater to, and as only few other companies continue to manufacture these products, the company focused their marketing efforts on this portfolio, resulting in increased acceptance and demand, thereby enhancing brand recognition for these products across their network of dealers.

Key Concerns:

- An inability to protect, strengthen and enhance existing brand could adversely affect the business prospects and financial performance.
- The continuing impact of the COVID-19 pandemic on business and operations is uncertain and it may be significant and continue to have an adverse effect on the business, operations and future financial performance.
- IPL engages in a highly competitive business and any failure to effectively compete could have a material adverse effect on it.
- May not be able to identify or effectively respond to evolving preferences, expectations or trends in a timely manner, and a failure to derive the desired benefits from product development efforts may impact the competitiveness and profitability.
- Ability to grow business depends on relationships with dealers and the community of painters, and any adverse changes in these relationships, or inability to enter into new relationships, could negatively affect the business and results of operations.
- IPL does not enter into long-term arrangements with dealers and any failure to continue its existing arrangements could negatively affect the business and results of operations.
- Under-utilization of manufacturing capacities and an inability to effectively utilize expanded manufacturing capacities could have an adverse effect on the business, future prospects and future financial performance.

- IPL’s proposed capacity expansion plans relating to its manufacturing facilities are subject to the risk of unanticipated delays in implementation and cost overruns.
- A significant portion of sales are derived from the state of Kerala and any adverse developments in this market could adversely affect the business.
- IPL has incurred borrowings from commercial banks and an inability to comply with repayment and other covenants in its financing agreements could adversely affect its business and financial condition.
- IPL does not have long-term agreements with its suppliers for raw materials, and an inability to procure the desired quality, quantity of its raw materials in a timely manner and at reasonable costs, or at all, may have a material adverse effect on its business, results of operations, financial condition, and cash flows.
- Any unscheduled or prolonged disruption of manufacturing operations could materially and adversely affect the business, financial condition, results of operations, and cash flows.
- Dependent on third-party transportation providers for the supply of raw materials and delivery of finished products.
- IPL is in the process of expanding operations and establishing a network of dealers in regions where it do not have a significant presence and prior experience. Any failure to expand into these new regions could adversely affect its sales, financial condition, result of operations, and cash flows.
- Stringent environmental, health and safety laws and regulations or stringent enforcement of existing environmental, health and safety laws and regulations may result in increased liabilities and increased capital expenditures.
- Business is working capital intensive. If IPL experience insufficient cash flows from its operations or are unable to borrow to meet working capital requirements, it may materially and adversely affect the business and results of operations.
- Inability to meet the quality standard norms prescribed by the central and state governments could result in the sales of IPL’s products being banned or suspended or becoming subject to significant compliance costs, which could have a material adverse effect on the business growth and prospects, results of operations, financial condition, and cash flows.
- Fluctuation in the prices of crude oil may affect IPL’s ability to price its products competitively.
- Improper storage, processing and handling of raw materials and finished products may cause damage to inventory leading to an adverse effect on the business, results of operations and cash flows.
- Business is subject to seasonal variations and cyclicality that could result in fluctuations in IPL’s results of operations.
- Inability to effectively manage growth or to successfully implement business plan and growth strategy could have an adverse effect on the business, results of operations, financial condition, and cash flows.
- Inability to accurately forecast demand or price for products and manage inventory may adversely affect the business, results of operations, financial condition, and cash flows.
- Inability to collect receivables and default in payment from dealers could result in the reduction of profits and affect the cash flows.
- Restrictions on import of raw materials may adversely impact the business and results of operations.
- Fluctuations in the average selling prices of its paint products could adversely affect the business, financial condition, results of operations, and cash flows.
- IPL may undertake strategic acquisitions or investments, which may prove to be difficult to integrate and manage or may not be successful.
- Faces foreign exchange risks that could adversely affect the results of operations and cash flows.
- Financial instability in other countries may cause increased volatility in Indian financial markets.

- Majority of the revenue is derived from business in India and a slowdown in economic growth in India could cause the business to suffer and could adversely affect the results of operations.

Profit & Loss

Particulars (Rs in Million)	H1FY21	FY20	FY19	FY18
Revenue from Operations	2594.2	6247.9	5356.3	4014.8
Other Income	8.2	16.4	16.3	16.3
Total Income	**2602.4**	**6264.4**	**5372.6**	**4031.1**
Total Expenditure	**2113.3**	**5338.0**	**4815.4**	**3756.7**
Cost of raw materials and components consumed	1238.2	3211.3	2965.2	2216.2
Purchase of traded goods	53.6	108.6	81.3	55.7
Decrease/ (increase) in inventories of finished goods and traded goods	60.3	-100.3	-61.2	40.9
Excise duty on sale of goods	0.0	0.0	0.0	64.0
Employee benefits expense	220.4	419.9	363.8	302.5
Other expenses	540.8	1698.5	1466.3	1077.4
PBIDT	**489.1**	**926.3**	**557.3**	**274.3**
Interest	24.7	56.0	46.6	45.4
PBDT	**464.4**	**870.4**	**510.7**	**228.9**
Depreciation	112.2	196.1	170.5	90.2
PBT	**352.3**	**674.3**	**340.2**	**138.7**
Exceptional items	0.0	0.0	3.1	13.2
Tax (incl. DT & FBT)	**80.2**	**196.1**	**68.4**	**-3.1**
Current tax	92.8	147.1	48.2	-3.1
Deferred tax (credit)/ charge	-12.6	49.0	20.2	0.0
PAT	**272.1**	**478.2**	**268.7**	**128.6**
EPS (Rs.)	9.4	16.5	9.3	4.5
Equity	290.2	290.2	288.5	285.9
Face Value	10.0	10.0	10.0	10.0
OPM (%)	18.5	14.6	10.1	6.4
PATM (%)	10.5	7.7	5.0	3.2

(Source:RHP)

Balance Sheet

Particulars (Rs in Million)	H1FY21	FY20	FY19	FY18
Non-current assets				
Property, plant and equipment	1403.5	1420.3	864.3	614.2
Right-of-use assets	271.59	278.0	311.4	97.2
Capital work-in-progress	25.8	10.9	44.0	24.6
Goodwill	305.5	305.5	305.5	407.4
Other intangible assets	4.7	3.7	4.3	4.9
Financial Assets				
Loans	58.0	54.8	40.7	6.9
Other financial assets	23.8	23.0	0.0	20.9
Income tax assets (net)	1.7	1.7	1.7	1.7
Other non-current assets	34.6	9.4	57.5	25.0
Total Non-Current Assets	**2129.2**	**2107.3**	**1629.5**	**1202.8**
Current assets				
Inventories	672.6	767.65	693.26	552.06
Financial Asset				
Investments	305.9	208.4	197.0	184.3
Trade receivables	855.7	1044.7	1038.5	967.9
Cash and cash equivalents	121.5	56.8	118.4	46.2
Bank Balances other than Cash and Cash Equivalents	0.0	0.0	21.8	0.2
Loans	5.6	3.2	3.3	2.6
Other financial assets	1.1	1.0	1.1	2.9
Other current assets	21.3	30.5	29.0	15.1
Total current Assets	**1983.7**	**2112.3**	**2102.4**	**1771.2**
Total Assets	**4112.9**	**4219.6**	**3731.8**	**2973.9**
EQUITY AND LIABILITIES				
Equity				

Equity share capital	290.2	290.2	288.5	285.9
Other Equity	1770.5	1497.3	1003.1	805.6
Instruments in the nature of equity	183.0	183.0	183.0	183.0
Total Equity	**2243.7**	**1970.5**	**1474.6**	**1274.6**
Non-current liabilities				
Financial liabilities				
Borrowings	193.3	247.2	269.1	89.1
Lease liabilities	25.7	28.2	54.1	48.3
Other liabilities	35.1	38.5	31.7	17.9
Deferred tax liabilities (net)	57.1	69.7	21.0	0.0
Provisions	27.9	13.0	0.0	0.0
Total Non-current liabilities	**339.1**	**396.5**	**375.9**	**155.3**
Current liabilities				
Trade payables				
Borrowings	0.0	145.3	247.1	226.4
Lease liabilities	31.8	34.4	39.9	28.8
Trade payables				
Total outstanding dues of micro and small enterprises	357.2	259.0	128.3	87.9
Total outstanding dues of creditors other than micro and small enterprises	833.9	1126.9	1234.1	997.4
Other financial liabilities	178.2	193.9	150.6	100.4
Other liabilities	85.0	56.1	78.3	101.6
Provisions	13.0	10.6	0.0	1.5
Income tax liabilities (net)	31.1	26.3	3.0	0.0
Total Current Liabilities	**1530.1**	**1852.5**	**1881.3**	**1544.0**
Total Liabilities	**1869.2**	**2249.1**	**2257.2**	**1699.3**
Total Equity and Liabilities	**4112.9**	**4219.6**	**3731.8**	**2973.9**

(Source:RHP)