PI Industries

Accumulate

Annual Report Analysis

Focusing on leveraging existing collaborations with the innovator companies in both the businesses – domestic agri-inputs and CSM exports. In domestic agri-inputs by entering into exclusive marketing rights of novel molecules in India with the innovators and in the CSM exports by deepening R&D capabilities, consequently resulting in commercialization of new molecules. To drive future growth company also hinted at venturing in business opportunities beyond agchem.

Entered into JV with Kuimai Chemicals to manufacture By-spriribac sodium (Nominee Gold) in India. Expect to start commercial manufacturing from FY19 onwards. Open to forming such JVs with innovators to launch novel molecules in India. Currently, PI has relationship with 18 global innovators. In addition to this, company establishing relationships with new companies to accelerate expansion into newer geographies and market segments.

Launched 5 products in FY18 – Header, Fender, Visma, Humesol and Elite. Key brands continue to be Nominee Gold, Osheen, Biovita, Cuprina, Roket, Foratox, Kitazin, Keefun and Vibrant. Plans to scale up new products launched in FY19, also intend to launch couple of more products in FY19. Expect Nominee Gold to continue to drive growth through deeper penetration across regions. In the CSM space commercialized 4 new molecules.

Osheen doubled - Osheen achieved 100% growth in FY18, PI has added 3 new co-marketing partners for Dinotefuron (Osheen's molecule) to expand the product further. While Nominee Gold expanded its customer base.

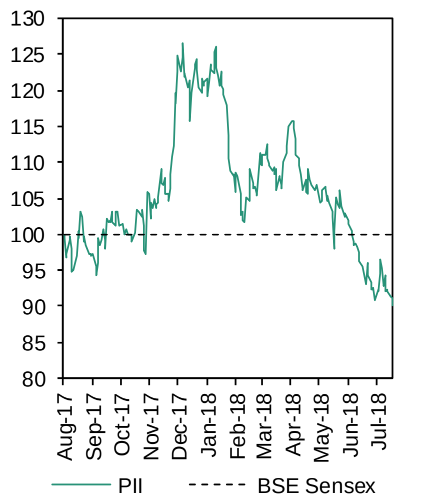
Looking to insulate China dependency - In order to reduce its dependency on Chinese raw material suppliers, PI looking to source raw materials from 6-7 alternate suppliers in India for few of its key products.

Payout decent at 15% - The dividend payout of Rs4/share (payout of 15% v/s 13% of FY17) in FY18, looks to strike a balance between cash retention and dividend payout. Retaining cash to fund future acquisitions and growth.

Tone Positive - Company expect to deliver growth in the coming years as new commercialised molecules scale up, capacity expansion at Jambusar, acceleration in pick-up of export shipments and company's continued investment in R&D. The company also believes looking at non agchem domain as well, upon fruition can provide sustainable growth for the company.

CMP	₹ 767
Target / Upside	₹ 878/14%
BSE Sensex	36,351
NSE Nifty	10,957
Scrip Details	
Equity / FV	₹ 138mn/₹1/-
Market Cap	₹ 107bn
	USD 1.6bn
52-week High/Low	₹ 1,035/674
Avg. Volume (no)	27,191
NSE Symbol	PIIND
Bloomberg Code	PI IN
Shareholding Pattern Mar'18 (%)	
Promoters	51.4
MF/Banks/FIs	19.0
FIIs	15.0
Public / Others	14.6

PII Relative to Sensex



FINANCIALS (₹ Mn)

Particulars	FY16	FY17	FY18	FY19E	FY20E
Net Sales	20,963	22,768	22,771	26,600	31,388
Growth (%)	8.2	8.6	0.0	16.8	18.0
EBITDA	4,312	5,533	4,934	5,825	6,905
OPM (%)	20.6	24.3	21.7	21.9	22.0
Net Profit	3,115	4,594	3,676	4,296	5,126
Growth (%)	26.7	47.5	(20.0)	16.9	19.3
EPS (₹)	22.7	33.4	26.7	31.2	37.2
Growth (%)	26.2	47.0	(20.2)	16.9	19.3
PER(x)	33.8	23.0	28.8	24.6	20.6
ROANW (%)	30.1	32.8	20.7	20.5	20.7
ROACE (%)	34.2	33.6	25.3	25.3	25.6

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July 19, 2018

Industry

Global agchem market continued to face headwinds

The global agchem market continued to face headwinds owing to lower crop prices, adverse climatic conditions in Brazil, higher channel inventories resulted in reduced expenditure on agrochemicals by farmers globally. Resulted in a decline in the global agchem market between CY13 to CY17. China supply constraints owing to environmental concerns was a double whammy. However, as per Phillips McDougall global agchem market is expected to grow by 4% over CY16 to CY20 to USD58.7b.

India fourth largest agrochemical market with a global market share of 10% at USD4.9bn in FY17, equally split between domestic and exports. The Indian agrochemical market is expected to grow at 7.5% CAGR per annum to reach USD 7.5bn by FY19. Insecticides continues to garner 60% of the market size followed by fungicides at 18%, herbicides 16% and rest from others.

Consolidation in the global agchem market – PI sees it as an opportunity

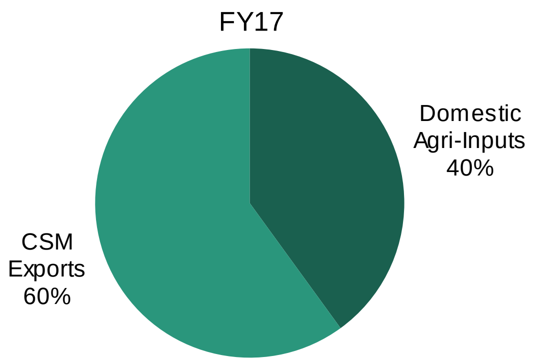
Rising environmental concerns and stricter government actions leading to consolidation and uncertainty in the Chinese chemical industries. Which is propelling global innovators to revisit their outsourcing strategy, where PI's business model fits.

Financial Performance

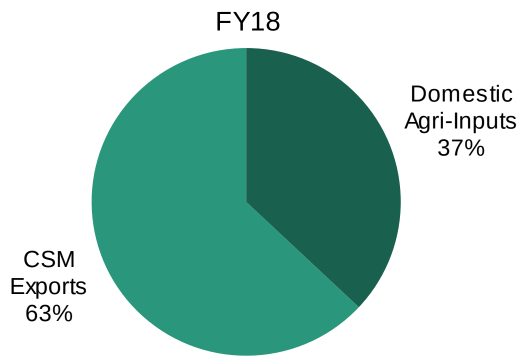
Domestic Agri-Inputs business dented blended revenue growth

Blended revenues (inclusive of excise duty) de-grew by 3% to ₹ 23bn, as domestic agri-inputs business witnessed a sharper de-growth of 10% to ₹ 8.5bn while CSM exports business saw marginal growth of a percent to ₹ 14.6bn. In terms of mix, because of de-growth in domestic agri input business, the segment's share in the total revenue mix contracted by 300bps to 37% while the CSM share increased by 300bps to 63% of the revenue mix.

Exhibit 1: Revenue mix

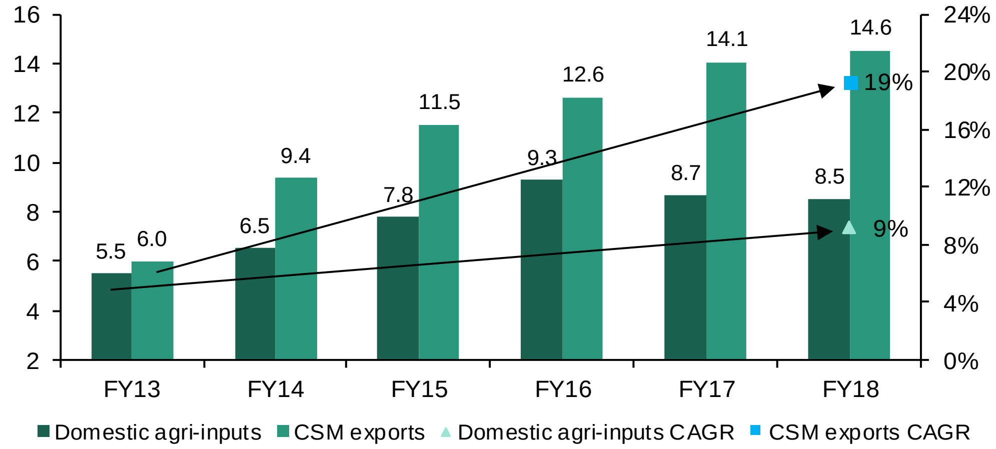


Source: Company, DART



Source: Company, DART

Exhibit 2: Segment revenue growth (₹ bn)

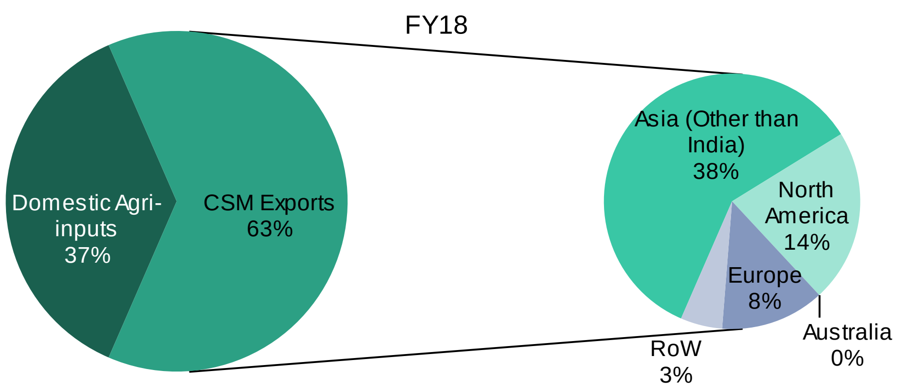


Source: Company, DART

Sharp de-growth in North America impacted CSM business revenues

Asia (ex-India) CSM revenues grew by 24% to ₹ 8.7bn while the revenue share of the region increased from 49% to 60% of the CSM revenues. North America CSM revenues saw a sharp de-growth of 41% to ₹ 3.2bn which led to fall in its contribution to the revenue mix from 38% to 22%. While Europe grew by 51% to ₹ 1.9bn with a revenue share of 13% increased from 9% while RoW grew by 79% to ₹ 0.8bn with a share of 5% increased from 3%. Australia which contributed ₹ 0.3bn in FY17, did not contribute anything in FY18.

Exhibit 3: CSM geographic revenue mix



Source: Company, DART

Exhibit 4: Region wise growth

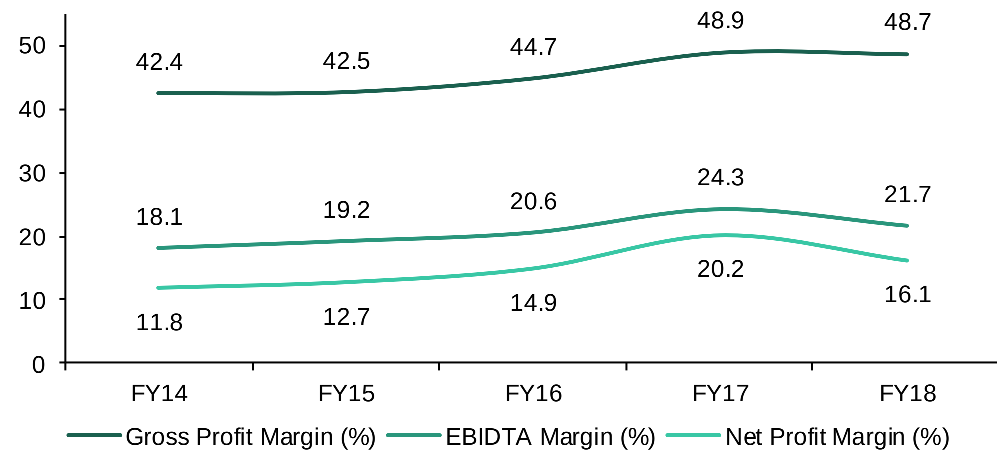
Geographical-Wise (₹ mn)	FY17	FY18	YoY (%)
Domestic Agri-inputs	**9,448**	**8,534**	**(10)**
India	9,448	8,534	(10)
CSM Exports	**14,385**	**14,553**	**1.2**
Asia (Other than India)	7,003	8,683	24
North America	5,406	3,191	(41)
Australia	279	0	(100)
Europe	1,268	1,911	51
RoW	429	769	79
Total Revenue	**23,833**	**23,087**	**(3.1)**

Source: Company, DART

Gross margins largely steady, negative operating leverage affected operating performance

Despite raw material supply constraints, PI was able to hold on to the strong gross margins of 48.7% with a marginal dip of 20bps. Precisely, because of its in-licensing business model. However, negative operating leverage led to EBITDA margin contraction of 263bps to 21.7% in FY18 and led to EBITDA de-growth of 11% to ₹ 4.9bn. Employee cost as a percentage of sales increased to 10.7% in FY18 from 9.8% in FY17 and other expenses as a percentage of sales shot up to 16.3% from 14.8%. Increase in tax rate from 9.8% in FY17 to 21% in FY18 led to net margin contraction of over 400bps to 16.1% in FY18.

Exhibit 5: Margin Analysis (%)

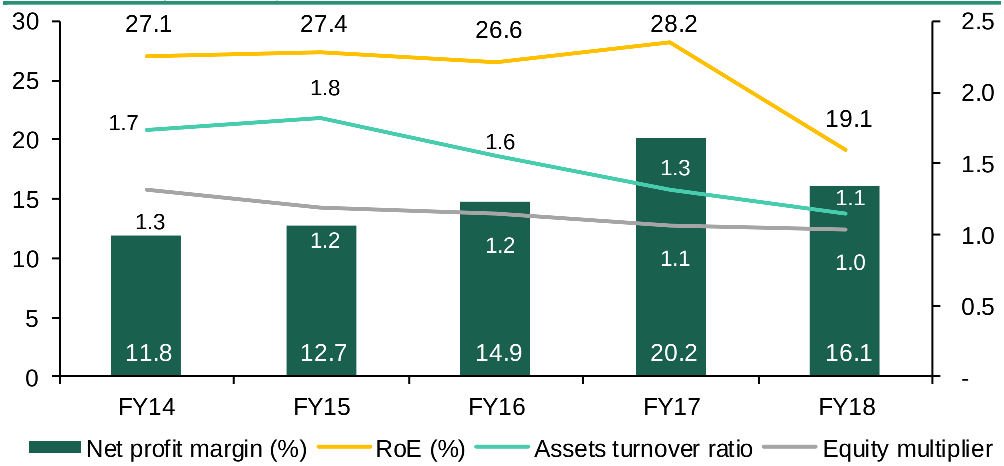


Source: Company, DART

DuPont analysis suggest deterioration in assets turnover led to contraction in RoE

Over FY14-18, RoE has contracted by 804bps to19.1%, we tried to dig deeper to get an understanding what led to the sharp contraction in the return on equity. The net margins over the same period expanded by 430bps to 16.1% while the asset turnover ratio has fallen from 1.7 in FY14 to 1.1 in FY18 (peaked in FY15 at 1.8) and the equity multiplier fall from 1.3 in FY14 to 1 in FY18. The utilization rate of the existing capacities has to pick up to drive return on equity going forward.

Exhibit 6: Dupont Analysis

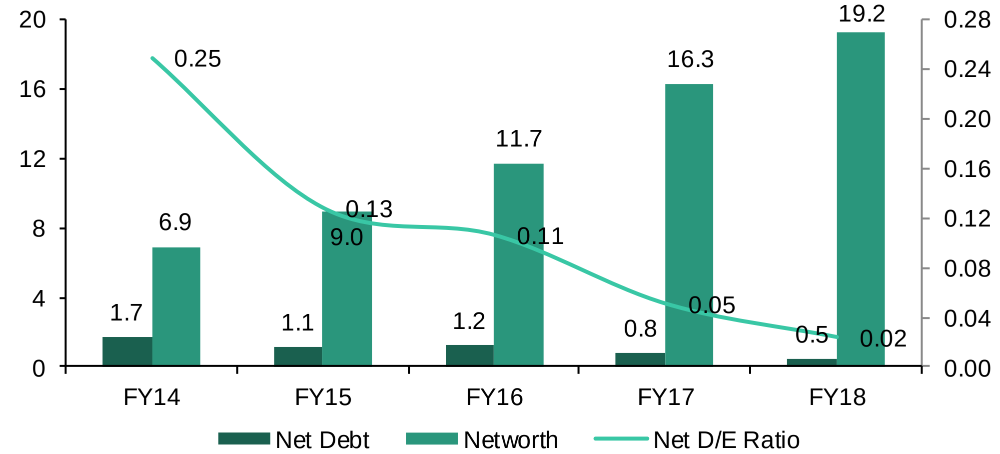


Source: Company, DART

Unlevered balance sheet gives substantial headroom to grow

PI continue to have a strong balance sheet with negligible debt on books to the tune of ₹ 463mn; due to strong cash flow generation PI was able to repay ₹ 364mn during the year. The debt equity ratio has fallen sharply from 0.25 to 0.02 in the last 5 years with the improvement in the networth coupled with repayment of debt over the years.

Exhibit 7: Declining leverage (₹ bn)

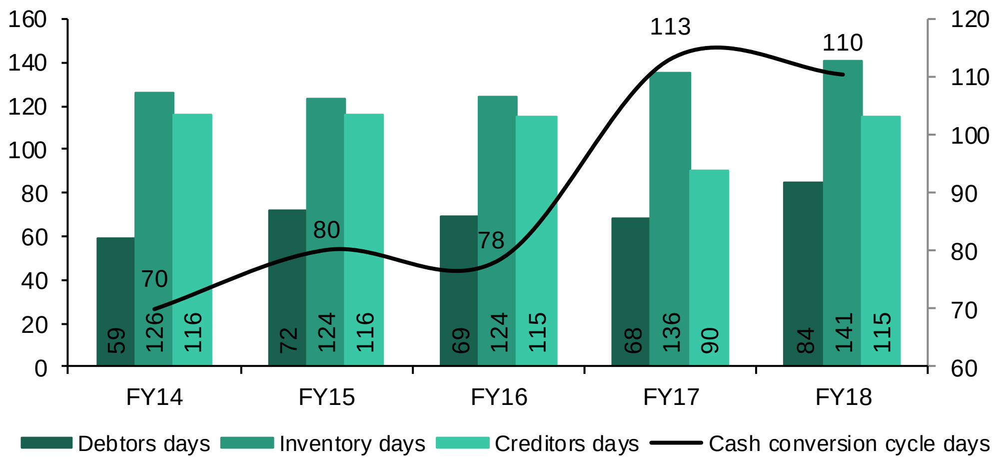


Source: Company, DART

Cash conversion cycle improved marginally

Working capital cycle improved in FY18 by 3 days to 110 days as increase in debtor and inventory days cumulative by 22 days, was offset by 25 days increase in payable days led to an improvement in cash conversion cycle by 3 days.

Exhibit 8: Working capital cycle

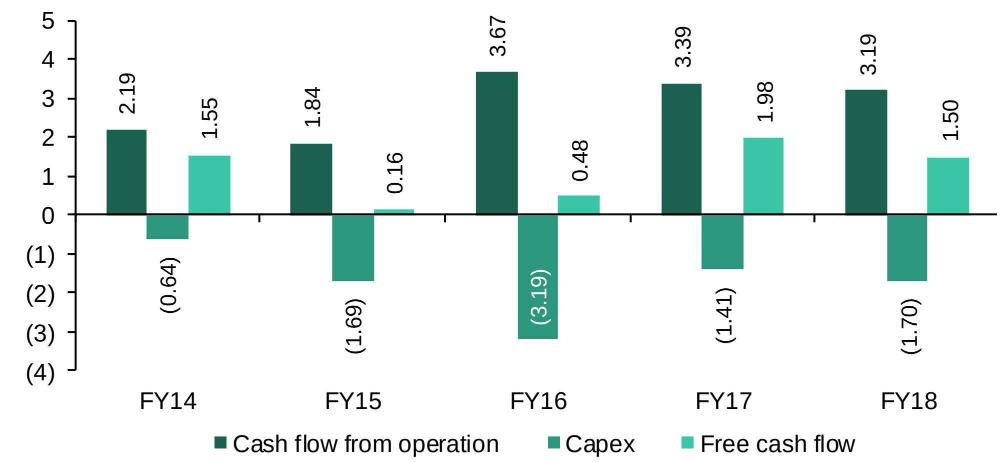


Source: Company, DART

Free cash flow generation continues to be strong

Despite incurring capex of ₹ 1.69bn, free cash flow generation was strong at ₹ 1.5bn though lower than FY17 as the quantum of capex in FY18 was higher. The company plans to do capex of ₹ 5bn over FY19-20 to set up new plants in Jambusar.

Exhibit 9: Free cash flow trend (₹ bn)

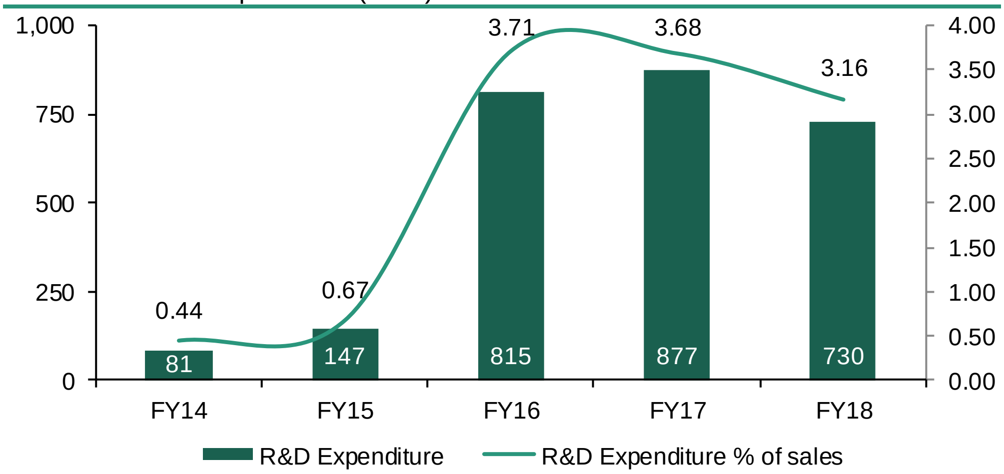


Source: Company, DART

R&D Expenditure over 3%

The total R&D expenditure in FY18 fell by 18% to Rs730mn, as a percentage of sales it contracted by 52bps to 3.2%. The capital expenditure on R&D accounted for 23% of the R&D expenditure while the rest is the revenue expenditure. As most of the capital expenditure on R&D was incurred last year. *(PI's R&D facility is based in Udaipur, Rajasthan with an area of 120,000 square feet. This facility is operated by 300 research scientists including more than 80 doctorates specializing in in-process research and complex chemistries.)*

Exhibit 10: R&D expenditure (₹ mn)



Source: Company, DART

Board structure independent while remuneration of KMPs at 3.5% of net income

The board comprises 8 directors out of which 6 are non-executive directors. Fairly an independent board structure. Remuneration paid to the key managerial personnel (MD and WTD) was ₹ 126mn accounting for 3.5% of the net profit of FY18.

Exhibit 11: Directors profile

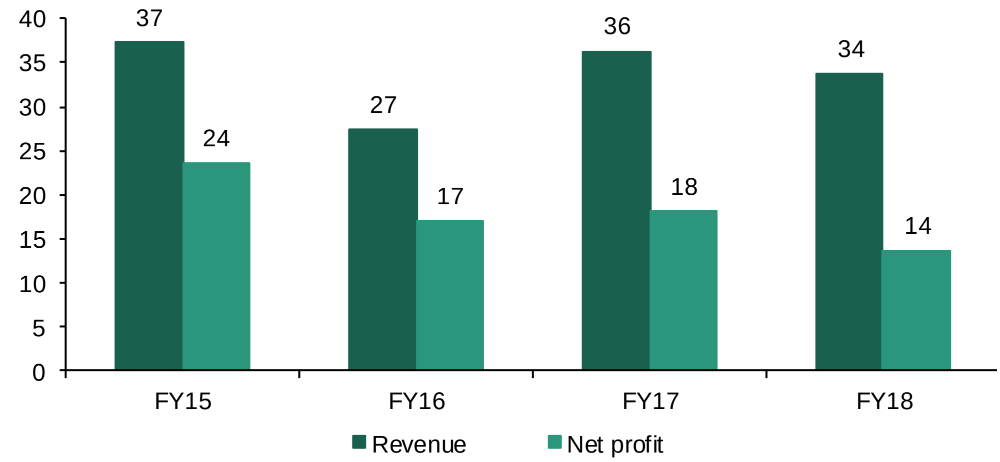
Name	Designation	Profile
Mr. Narayan K. Seshadri	Chairman & Independent Director	A chartered accountant, with an expertise in strategic planning and financial engineering. Besides PI he is also chairman of Magma Fincorp and Astra zeneca pharma. He also serves on the boards of 15 companies.
Mr. Mayank Singhal	**Managing Director & CEO**	**He is an engineering management graduate from the UK with over 20 years of experience in agchem industry. He also serves on the boards of 5 companies.**
Mr. Rajnish Sarna	**Whole-time Director**	**He is chartered accountant with more than 25 years of experience in strategy, finance & risk management, investor relation and corporate planning & reporting. He also serves on the boards of 4 other companies.**
Mr. Pravin K. Laheri	Independent Director	Graduated from law and a retired IAS officer (Gujarat cadre). He served the govt. of Gujarat in various positions. He also serves on the board of 9 other companies.
Ms. Ramni Nirula	Independent Director	An MBA from Delhi university and have an over 3 decades of experience in the financial industry. She also serves on the board of 8 other companies.
Mr. Ravi Narain	Independent Director	He holds master's degree in economics and a degree in Business Administration. He is currently Non-Executive Vice Chairman of the NSE. He also serves on the board of 2 companies.
Mr. Arvind Singhal	Non-Executive, Non-Independent Director	He is an entrepreneur with more than 4 decades of experience. He has been actively associated with business chambers like federation of Indian Mineral Industries (fIMI), CII, FICCI and ASSOCHAM. He also serves on the board of 7 companies.
Dr T.S. Balganesh	Independent Director	He holds the PhD in Medical Microbiology and have more than 3 decades of experience in antibacterial drug discovery. He also serves on the board of 2 companies.

Source: Company, DART

Subsidiaries performance

PI has 3 subsidiaries – PI Life Science Research Ltd, PI Japan Co. ltd and PIIL Finance and Investment Ltd. All the 3 subsidiaries posted profit during the year. PI Life Science posted a profit of ₹ 13.7 mn on account of R&D activities for developing new products. PIIL Finance and Investments ltd reported a profit of ₹ 2.4mn and PI Japan Co. Ltd reported a profit of JPY 3.1mn in FY18.

Exhibit 12: PI Life Science Research Ltd. performance (₹ mn)



Source: Company, DART

Marginal decline in promoter holding

The promoter holding declined marginally from 51.6% to 51.4%. While the new institutional entrants were DSP Blackrock and Amansa Holdings while ICICI MF almost doubled its stake from 3.38% to 5.33%. Cartica Caital, Smallcap World Fund Inc and Oppenheimer International Small Company Fund which were holding 6.17%, 1.88% & 1.89 each completely exited the company.

Exhibit 13: Promoter holding and top holders

% Outstanding	FY17	FY18
Promoter	51.55	51.4
Others		
ICICI Prudential value discovery fund	3.38	5.33
SBI Blue Chip Fund	3.08	3.44
Axis Mutual Fund A/c Axis Long Term Equity Fund	3.56	3.05
DSP Blackrock A.C.E fund Series = 1	-	2.02
UTI Mahila Unit Scheme	0.97	1.86
Amansa Holdings Pvt. Ltd.	-	1.82
Franklin Templeton Mutual Fund A/c Franklin India	0.8	1.51
Stichting Depositary APG Emerging Markets Equity Pool	1.16	1.16
Government Pension Fund Global	1	0.98
Rowanhill Investments Ltd	0.8	0.79
India Emerging Opportunities Fund Ltd	0.95	0.67
Cartica Capital Ltd.	6.17	-
Smallcap World Fund, Inc	1.88	-
Oppenheimer International Small Company Fund	1.89	-

Source: Company, DART

Income Statement (₹ mn)

Particulars	Mar17	Mar18	Mar19E	Mar20E
Net Sales	**22,768**	**22,771**	**26,600**	**31,388**
Other income	366	602	532	628
Total Income	**23,134**	**23,373**	**27,132**	**32,016**
Total Expenditure	**17,236**	**17,837**	**20,775**	**24,483**
Raw Material Consumption	11,632	11,690	13,593	16,071
Employee Expenses	2,226	2,432	2,713	3,170
Other Expenses	3,378	3,715	4,469	5,242
EBIDTA (Excl. OI)	**5,533**	**4,934**	**5,825**	**6,905**
EBIDTA (Incl. OI)	**5,899**	**5,536**	**6,357**	**7,533**
Interest	72	53	63	42
PBDT	**5,827**	**5,483**	**6,294**	**7,491**
Depreciation	730	830	856	1,006
PBT & EO Items	5,095	4,655	5,438	6,485
PBT	**5,095**	**4,655**	**5,438**	**6,485**
Tax	501	979	1,142	1,362
Net Profit	**4,594**	**3,676**	**4,296**	**5,126**

Balance Sheet (₹ mn)

Particulars	Mar17	Mar18	Mar19E	Mar20E
Sources of Funds				
Equity Capital	138	138	138	138
Share Premium	1,909	1,984	1,984	1,984
Other Reserves (excl Sh. P)	14,225	17,126	20,468	24,712
Net Worth	**16,272**	**19,248**	**22,591**	**26,834**
Revaluation reserve	0	0	20	20
Loan Funds	**830**	**463**	**900**	**600**
Other Liabilities	172	183	0	0
Total Capital Employed	**17,273**	**19,895**	**23,511**	**27,454**
Applications of Funds				
Gross Block	12,415	12,067	14,267	16,767
Less: Accumulated Dep	2,965	2,090	2,946	2,946
Net Block	**9,450**	**9,977**	**11,321**	**13,821**
Capital Work in Progress	773	899	0	0
Investments	833	1,607	833	833
Current Assets, Loans & Advances				
Inventories	4,319	4,520	5,101	6,020
Sundry Debtors	4,237	5,268	5,466	6,450
Cash and Bank Balance	844	1,172	5,322	5,603
Other Bank balance	482	134	0	0
Loans and Advances	118	76	160	160
Other Current Assets	1,956	2,612	2,200	2,200
sub total	11,958	13,782	18,249	20,432
Less: Current Liabilities & Provisions				
Current Liabilities	5,425	6,029	6,092	6,832
Provisions	316	340	800	800
sub total	5,741	6,369	6,892	7,632
Net Current Assets	6,217	7,413	11,357	12,800
Total Assets	**17,273**	**19,895**	**23,511**	**27,454**

E – Estimates

Cash Flow (₹ mn)

Particulars	Mar17	Mar18	Mar19E	Mar20E
Profit before tax	5,095	4,655	5,438	6,485
Depreciation & w.o.	730	830	856	1,006
Net Interest Exp	(84)	(213)	63	42
Direct taxes paid	(1,212)	(963)	(1,142)	(1,362)
Change in Working Capital	(1,235)	(1,044)	205	(1,162)
Other	94	(71)	(314)	(1,002)
(A) CF from Opt. Activities	**3,388**	**3,194**	**5,106**	**4,007**
Capex	(1,413)	(1,696)	(1,301)	(2,500)
Free Cash Flow	**1,976**	**1,498**	**3,805**	**1,507**
Inc./ (Dec.) in Investments	(1,095)	(375)	774	0
Other (Bal fig)	157	266	0	0
(B) CF from Invt. Activities	**(2,351)**	**(1,805)**	**(528)**	**(2,500)**
Issue of Equity/ Preference	83	19	0	0
Inc./(Dec.) in Debt	(297)	(364)	437	(300)
Interest exp net	(72)	(53)	(63)	(42)
Dividend Paid (Incl. Tax)	(248)	(662)	(803)	(884)
(C) CF from Financing	**(534)**	**(1,060)**	**(430)**	**(1,226)**
Net Change in Cash	503	328	4,149	282
Opening Cash balances	342	844	1,173	5,322
Closing Cash balances	844	1,173	5,322	5,604

Important Ratios

Particulars	Mar17	Mar18	Mar19E	Mar20E
(A) Measures of Performance (%)				
Gross Profit Margin	48.9	48.7	48.9	48.8
EBIDTA Margin (excl. O.I.)	24.3	21.7	21.9	22.0
Interest / Sales	0.3	0.2	0.2	0.1
Tax/PBT	9.8	21.0	21.0	21.0
Net Profit Margin	20.2	16.1	16.2	16.3
(B) As Percentage of Net Sales				
Raw Material	51.1	51.3	51.1	51.2
Employee Expenses	9.8	10.7	10.2	10.1
Other Expenses	14.8	16.3	16.8	16.7
(C) Measures of Financial Status				
Debt / Equity (x)	0.05	0.02	0.04	0.02
Interest Coverage (x)	81.9	104.1	100.9	179.4
Average Cost of Debt (%)	6.9	8.2	9.2	5.6
Debtors Period (days)	67.9	84.4	75.0	75.0
Closing stock (days)	135.5	141.1	137.0	136.7
Payable Days	90.3	115.1	88.1	87.9
Inventory Turnover (x)	5.3	5.0	5.2	5.2
Fixed Assets Turnover (x)	1.8	1.9	1.9	1.9
WC Turnover (x)	3.7	3.1	2.3	2.5
Non Cash WC (₹ Mn)	5,373	6,240	6,035	7,197
(D) Measures of Investment				
EPS (₹) (excl EO)	33.4	26.7	31.2	37.2
CEPS (₹)	38.7	32.7	37.4	44.5
DPS (₹)	4.0	4.0	5.0	5.5
Dividend Payout (%)	12.0	15.0	16.0	14.8
Profit Ploughback (%)	88.0	85.0	84.0	85.2
Book Value (₹)	118.3	139.6	163.8	194.6
RoANW (%)	32.8	20.7	20.5	20.7
RoACE (%)	33.6	25.3	25.3	25.6
RoAIC (%)	35.0	26.8	29.8	32.6
(E) Valuation Ratios				
CMP (₹)	767	767	767	767
P/E (x)	23.0	28.8	24.6	20.6
Market Cap. (₹ Mn)	105,816	105,816	105,816	105,816
MCap/ Sales (x)	4.6	4.6	4.0	3.4
EV (₹ Mn)	105,801	105,107	101,394	100,813
EV/Sales (x)	4.6	4.6	3.8	3.2
EV/EBDITA (x)	19.1	21.3	17.4	14.6
P/BV (x)	6.5	5.5	4.7	3.9
Dividend Yield (%)	0.5	0.5	0.7	0.7

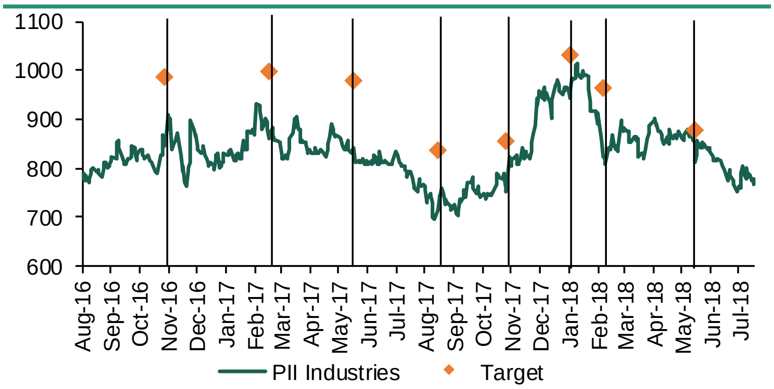
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	**> 20%**
Accumulate	**10 to 20%**
Reduce	**0 to 10%**
Sell	**< 0%**

Rating and Target Price History



Month	Rating	TP (₹)	Price (₹)*
Oct'16	Buy	990	845
Feb'17	Accumulate	1,001	872
May'17	Accumulate	980	843
Aug'17	Accumulate	840	712
Oct'17	Accumulate	856	753
Jan'18	Accumulate	1,034	961
Feb'18	Accumulate	965	820
May'18	Accumulate	878	812

** As on Recommendation Date*

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