Sharekhan by BNP PARIBAS

PI Industries

Healthy performance continues, Upgrade to Buy

Sector: Agri Chem
Result Update

	Change
Reco: **Buy**	↑
CMP: **Rs. 1,547**	
Price Target: **Rs. 1,750**	↑

↑ Upgrade ↔ No change ↓ Downgrade

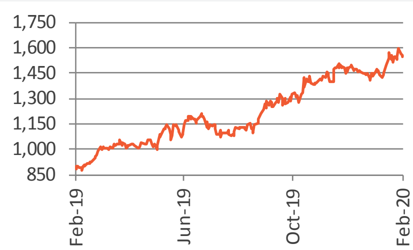
Company details

Market cap:	Rs. 21,363 cr
52-week high/low:	Rs. 1,626/864
NSE volume: (No of shares)	1.4 lakh
BSE code:	523642
NSE code:	PIIND
Sharekhan code:	PIIND
Free float: (No of shares)	6.7 cr

Shareholding (%)

Promoters	51
FII	14
DII	21
Others	14

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	8.8	10.1	38.6	76.3
Relative to Sensex	8.9	6.8	25.1	51.7

Sharekhan Research, Bloomberg

PI Industries Limited (PI Industries) delivered revenue growth of 20.1% y-o-y to Rs. 850 crore during Q3FY2020, led by robust revenue growth of 24% y-o-y in domestic business and continued ramp-up in exports (up by 19% y-o-y). Gross margin remained at similar levels of 46.6%, however operating margins improved by 94 BPS y-o-y to 21.9% owing to economies of scale as other operating cost was down by 96 BPS to 15.7% of sales as compared to 16.6% during Q3FY2019. Healthy revenue growth and improvement in operating margin led to 25.5% growth in EBITDA at Rs. 187 crore. However, increased depreciation (up by 36.3% y-o-y) restricted PBT growth in PBT to 22.3% despite other income being higher by 25.7% y-o-y. Higher tax incidence of 28.7% in Q3FY2020 as against 22.8% in Q3FY2019 further restricted growth in PAT to 13.0% to Rs. 121 crore. Management has retained its FY2020E guidance of ~20% y-o-y improvement in performance, led by healthy order book, commissioning of additional capacity and contribution from newly launched brands. The Board has also approved an enabling resolution to raise funds upto Rs. 2,000 crore so as to support the next phase of growth.

Key positives

- Robust revenue growth of 24% y-o-y in domestic business (largely volume driven) and continued ramp-up in exports (up by 19% y-o-y).
- OPM expanded by 94 BPS to 21.9%, led by economies of scale and cost efficiencies.

Key negatives

- Export order book remained flat at US$ 1.4 billion.

Our Call

Valuation: Aggressive expansion strategy to tap the robust and encouraging demand environment – Upgrade to Buy: We expect revenue and earnings CAGR of 27.6% and 29.8%, respectively, during FY2019-FY2022E (Isagro numbers factored in from Q4FY2020). At the current market price, the stock is trading at 40.2x/28.9x/23.8x its FY2020E/FY2021E/FY2022E earnings. With industry-leading return ratios, healthy balance sheet and strong earnings visibility; we expect the stock to continue to fetch premium valuations. We upgrade our rating on the stock to Buy with a revised PT of Rs. 1,750 per share owing to aggressive expansion strategy to tap the robust and encouraging demand environment.

Key Risks

- Delay in commissioning of projects or execution of orders or delayed orders by clients in the CSM business can affect revenue growth.
- Higher-than-normal time lag in passing on the increase in raw-material prices could affect margins.

Valuation (consolidated) Rs cr

Particulars	FY18	FY19	FY20E	FY21E	FY22E
Revenues	2,277	2,841	3,528	4,844	5,902
OPM (%)	21.7	20.3	21.2	21.5	21.7
Adjusted PAT	368	410	529	737	896
% y-o-y growth	*(20.0)*	*11.5*	*29.1*	*39.4*	*21.5*
Adjusted EPS (Rs.)	26.7	29.8	38.5	53.6	65.1
P/E (x)	57.9	51.9	40.2	28.9	23.8
P/B (x)	11.1	9.3	7.7	6.2	5.0
EV/EBITDA (x)	42.6	36.6	28.3	20.2	16.2
RoNW (%)	20.7	19.5	21.0	23.8	23.2
RoCE (%)	25.0	24.9	27.1	30.7	29.9

Source: Company; Sharekhan estimates

Healthy performance continues: PI Industries delivered revenue growth of 20.1% y-o-y to Rs. 850 crore (broadly in-line with our estimate of Rs. 862 crore), led by robust revenue growth of 24% y-o-y in domestic business (largely volume driven) and continued ramp-up in exports (up by 19% y-o-y). The company witnessed increased revenue in the domestic market owing to higher acreages across key products during Rabi season, which led to healthy demand off-take of the company products (increased volumes sold). Newly launched wheat herbicide 'Awkira' has been showing promising results. Gross margin remained at similar levels of 46.6%; however, operating margins improved by 94 BPS y-o-y to 21.9% (similar to our expectation of 21.9%) owing to economies of scale as other operating cost was down by 96 BPS to 15.7% of sales as compared to 16.6% during Q3FY2019. Healthy revenue growth and improvement in operating margin led to 25.5% growth in EBITDA at Rs. 187 crore. However, increased depreciation (up by 36.3% y-o-y) restricted PBT growth to 22.3% despite other income being higher by 25.7% y-o-y. Further, higher tax incidence of 28.7% in Q3FY2020 as against 22.8% in Q3FY2019 (owing to change in SEZ share to overall business) further restricted PAT growth to 13.0% at Rs. 121 crore (broadly in line with our estimate of Rs. 124 crore).

Aggressively enhancing manufacturing capability owing to robust demand environment in exports: Management highlighted that owing to strong demand from export markets (export order book remained stagnant at $1.4 billion despite strong revenue growth implying a healthy order intake), the company is ramping up its capex programme. The multi-purpose plant in Jambusar facility (largely for backward integration and a new technology block) is slated to be commissioned in Q4FY2020. Three facilities are slated to be commissioned in FY2021E, one each in Q1FY2021, Q2FY2021 and Q3FY2021 or Q4FY2021. The company had outlined capex of Rs. 600 crore for FY2020 (Rs. 550 crore incurred till date) and Rs. 250 crore-300 crore for FY2021E. Management stated that asset-turnover ratio should be at 1.25x-1.75x for the new capacities; however, peak asset turnover should be reached in 12-18 months post commissioning at an utilisation level of 80-85%. The company is expected to fund the capex through internal accruals as operating cashflow generation is expected to remain robust; hence, reliance on external funding seems negligible.

Highlights of Q3FY2020 Results concall

- **Focus on enhancing R&D capabilities continues:** As the number of enquires is increasing at a rapid pace, the pipeline in R&D activity is also increasing (recent development in China is one of the reasons for such surge in enquires). Scientist work on the technology shared by the customers in the CSM business along with working on the own proprietary molecules developed in-house. During the quarter, the company developed three new molecules in the CSM business, taking total molecules to 21. Management also stated that run-rate of 2-3 new product launches each year is expected to continue going forward as well.
- **H2 always better than H1:** Management highlighted that demand patterns are such that H2 performance is healthy as compared to H1 and sees no change this time as well.
- **Effective tax rate:** Management has guided for an effective tax rate of 25-26% for FY2020 and stated that it will evaluate the pros and cons of moving into the new tax rate regime for FY2021 as significant expansion plans are ongoing and it also has a facility in SEZ.
- **Lower dependence on China:** Management stated that the company has a lower dependence on China as revenue dependence is less than 10%. Further, over a period of time, the company has reduced vendor concentration to selected few as it diversified its raw-material sourcing from various suppliers situated in different geographies. Hence, management believes that outbreak of Corona virus in China is unlikely to have a significant impact on the company's overall performance.
- **Management retains its FY2020 guidance:** Though the accident at Jambusar facility is likely to have an adverse impact of Rs. 40 crore-50 crore on revenue during Q4FY2020, management believes that from the medium to long term perspective, it will not impact the business performance. Management has retained its FY2020E guidance of ~20% y-o-y improvement in performance, led by healthy order book, commissioning of additional capacity and contribution from newly launched brands.

- **Utilisation of surplus cash:** Healthy performance led to robust operating cash flow generation, which further strengthened the balance sheet. Hence, the company utilised the surplus cash in acquisition of balance stake in Isagro Asia along with capacity expansion at it Jambusar facility.
- **Amalgamation of Isagro Asia:** Post the acquisition of balance stake, Isagro Asia has become a wholly owned subsidiary of PI Industries and now it has been decided that it would merge Isagro Asia into PI Industries excluding the domestic distribution business, which will be transferred to Jivagro Limited.
- **Passed an enabling resolution to raise Rs. 2,000 crore:** To support the next phase of growth, the board approved an enabling resolution for raising funds upto Rs. 2,000 crore. Growth is expected to be led by either i) organic business growth through aggressive capacity expansion, ii) inorganic acquisition to acquire new and niche technological capabilities (either in domestic market or overseas), and iii) to diversify into adjacent verticals such as pharmaceuticals, hi-tech speciality chemicals, Nutraceuticals etc. or a combination of all.
- **Interim dividend:** The board has approved interim dividend of 300% on face value of Rs. 1 each, i.e. Rs 3/ share.

Results Rs cr

Particulars	Q3FY20	Q3FY19	YoY (%)	Q2FY20	QoQ (%)
Net Sales	**850**	**708**	**20.1**	**907**	**(6.3)**
Material Cost	454	378	20.2	522	(13.1)
Gross Profit	**396**	**330**	**20.0**	**385**	**2.9**
Employee Expenses	76	64	19.9	73	4.9
Other Expenses	133	118	13.2	120	11.2
EBITDA	**187**	**149**	**25.5**	**193**	**(3.1)**
Other Income	19	15	25.7	11	75.2
Depreciation	32	23	36.3	32	0.6
Interest	4	2	153.3	3	52.0
PBT	**170**	**139**	**22.3**	**169**	**0.4**
Tax	49	32	54.1	46	5.6
RPAT	**121**	**107**	**13.0**	**123**	**(1.5)**
EPS (Rs)	8.8	7.8	13.0	8.9	(1.5)
%			**YoY (BPS)**		**QoQ (BPS)**
Gross profit margin	46.6	46.6	(3)	42.4	417
EBITDA margin	21.9	21.0	94	21.2	73
Net margin	14.3	15.2	(90)	13.6	70

Source: Company; Sharekhan Research

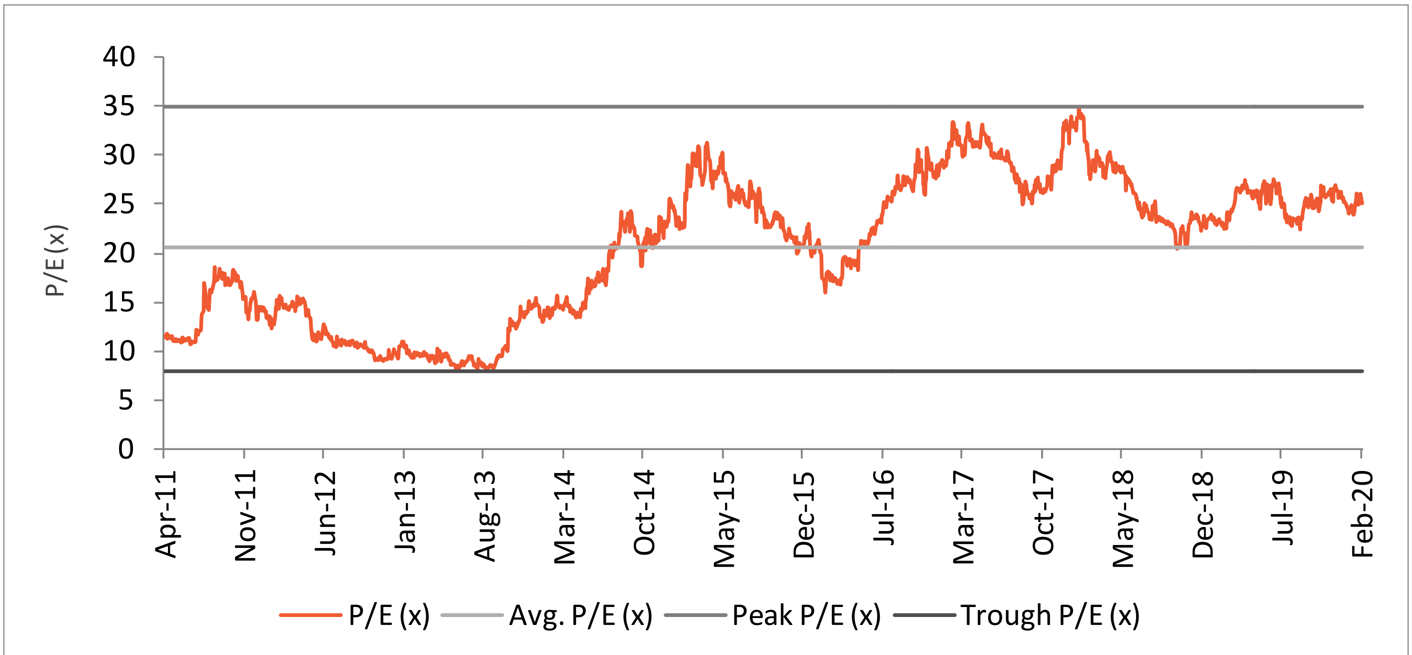
Outlook

Retains guidance of 20% revenue growth in FY2020: Management highlighted that the demand pattern is such that the performance in H2 is healthy as compared to H1 and sees no change this time as well. Hence, it retains its FY2020E guidance of ~20% y-o-y improvement in performance led by healthy order book, commissioning of additional capacity and contribution from newly launched brands. The company had outlined a capex of Rs. 600 crore for FY2020 (Rs. 550 crore incurred till date) and Rs. 250 crore-300 crore for FY2021E. Three facilities are slated to be commissioned in FY2021E, one each in Q1FY2021, Q2FY2021 and Q3FY2021 or Q4FY2021.

Valuation

Aggressive expansion strategy to tap the robust and encouraging demand environment – Upgrade to Buy: We expect revenue and earnings CAGR of 27.6% and 29.8%, respectively, during FY2019-FY2022E (Isagro numbers factored in from Q4FY2020). At the current market price, the stock is trading at 40.2x/28.9x/23.8x its FY2020E/FY2021E/FY2022E earnings. With industry-leading return ratios and a healthy balance sheet and strong earnings visibility, we expect the stock to continue to fetch premium valuations. We upgrade our rating on the stock to Buy with a revised PT of Rs. 1,750 per share owing to aggressive expansion strategy to tap the robust and encouraging demand environment.

One-year forward P/E (x) band – Trades at rich valuation, upside looks limited



Source: Sharekhan Research

About company

Incorporated in 1947, PI Industries focuses on developing complex chemistry solutions in agri-sciences with an integrated approach. The company currently operates a strong infrastructure setup, consisting of three formulation facilities and nine multi-product plants under its three manufacturing facilities. These state-of-the-art facilities have integrated process development teams with in-house engineering capabilities. The company also maintains a strong research presence through its R&D facility at Udaipur and has a dedicated team of over 250 scientists and chemists.

Investment theme

A strong CSM order book of $1.4 billion at the end of Q3FY2020 provides healthy revenue visibility. Management foresees encouraging outlook for the CSM business as business sentiments improve globally for products, wherein the company operates. The company had outlined capex of Rs. 600 crore for FY2020 (Rs. 550 crore incurred till date) and Rs. 250 crore-300 crore for FY2021E. Three facilities are slated to be commissioned in FY2021E, one each in Q1FY2021, Q2FY2021 and Q3FY2021 or Q4FY2021.

Key Risks

- Delay in commissioning of projects or execution of orders or deferral of orders by clients in the CSM business can affect revenue growth.
- Higher-than-normal time lag in passing on the increase in raw-material prices could affect margins.

Additional Data

Key management personnel

Narayan K. Seshadri	Non-Executive & Independent Chairperson
Dr. Raman Ramachandran	Managing Director & Chief Executive Officer
Mr. Mayank Singhal	Executive Director
Mr. Rajnish Sarna	Executive Director
Arvind Singhal	Non-Executive - Non Independent Director
Subhash Anand	Chief Financial Officer
Naresh Kapoor	Company Secretary & Compliance officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Jackson National Asset Management	5.11
2	ICICI Prudential Asset Management	4.47
3	SBI Funds Management Pvt Ltd	4.07
4	SBI LARGE MIDCAP FUND	4.03
5	Cartica Capital Ltd	3.50
6	UTI Asset Management Co Ltd	1.88
7	Franklin Templeton Mutual	1.81
8	DSP Investment Managers Pvt Ltd	1.44
9	Stichting Depository Apg Emerging Market	1.41
10	Vanguard Group Inc	1.35

Source: Bloomberg

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