Sharekhan by BNP PARIBAS

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Insecticides (India) Limited

New products to revive growth momentum

Agri Chem	Sharekhan code: INSECTICID	Result Update

Stock Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)		✓	
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 489**	
Price Target: **Rs. 590**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 1,010 cr
52-week high/low:	Rs. 568/207
NSE volume: (No of shares)	0.7 lakh
BSE code:	532851
NSE code:	INSECTICID
Free float: (No of shares)	0.64 cr

Shareholding (%)

Promoters	69
DII	12
FII	4
Others	15

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	3.8	9.7	6.1	0.1
Relative to Sensex	-0.4	-10.8	-28.4	-25.2

Sharekhan Research, Bloomberg

Summary

- Q3FY2021 results were weak as OPM missed by 306 bps at 5% (down 370 bps y-o-y); it led PAT to be 46% lower than expected at Rs. 6 crore (down 30.9% y-o-y). OPM shrunk due to a 492 bps y-o-y decline in gross margins to 21.1% (high raw material cost & rise in higher share of low margin generic products) and increase in logistic cost.
- Although revenues grew by 13.8% y-o-y to Rs. 299 crore, the mix deteriorated as share of branded products declined by 668 bps y-o-y to 68.8% while that of low margin institutional sales increased by 743 bps y-o-y to 26.4%.
- Management guided for 15% revenue growth for FY2022 led by new launches and expects gross margin to recover gradually to historical level of 29-30% supported by backward integration, product price hikes and rise in share of high-margin products.
- We maintain a Buy on Insecticides (India) with a revised PT of Rs. 590 as we expect strong earnings recovery (PAT to clock 38% CAGR over FY21E-FY23E) along with decent RoE of 15-16%. At CMP, stock is trading at an attractive valuation of 6.6x FY2023E EPS.

Insecticides (India) Limited's Q3FY2021 revenues increased by 13.8% y-o-y to Rs. 299 crore, which was 11% above our estimate of Rs. 268 crore. The revenue growth was driven by 3.7% y-o-y rise in total branded sales to Rs. 206 crore, a 58.4% y-o-y rise in institutional sales while exports declined by 1.4% y-o-y. Branded sales improved due to 6.8% y-o-y growth in Maharatna sales and 1.4% y-o-y increase in other branded sales. However, OPM shrunk by 370 bps to 5% (306 bps lower than our estimate of 8.1%) due to a decline in gross margin by 492 bps to 21.1% (given higher raw material cost), rise in share of low-margin generic products and a increase in logistics cost. Consequently, operating profit fell by 34.4% y-o-y to Rs. 15 crore, below our estimate of Rs. 22 crore. Adjusted PAT declined by 31% y-o-y to Rs. 6.1 crore, below our estimate of Rs. 11 crore due to weaker-than-expected margins. The management guided for strong a 15% revenue growth for FY2022 with the ramp-up of revenues (most new products at 50% of revenue potential and target is to take it to 75-80%) from new products (launched 7 new products in 9MFY2021 and plan to launch another three products in Q4FY2021). Moreover, margins are also expected to recover (from dismal performance of 9MFY21) on back of backward integration (10-15% saving in raw material costs), likely product price hikes and rise in share of high-margin new products. We thus expect strong 38% PAT CAGR over FY2021E-FY2023E along with decent RoE of 15-16%. Hence, we maintain a Buy on Insecticides (India) with a revised PT of Rs. 590.

Key positives

- Revenues increased by 13.8% y-o-y led by higher institutional sales (up 58.4% y-o-y).
- Company had net cash of Rs. 35 crore as of December 2020.

Key negatives

- OPM shrunk by 370 bps y-o-y to only 5% (versus our estimate of 8.1%) due to a sharp decline in gross margins (weak product mix and high raw material cost) and a rise in logistics cost.

Our Call

Valuation – Maintain Buy on Insecticides (India) with a revised PT of Rs. 590: We have lowered our FY2021 earnings estimate to factor in a weaker-than-expected margin performance in Q3FY2021 and have fine-tuned our FY2022-FY2023 earnings estimates. We believe that revenue growth momentum would pick up with a ramp-up in revenue contribution from new products, while backward integration and potential increase in product prices price would take gross margins back to historical level of ~29-30% by FY2023E. We thus expect strong revenue, EBITDA and PAT CAGR of 10%/33%/38% over FY2021E-FY2023E (owing to low base in FY2021 due to COVID-19) along with a decent RoE of 15-16%. Hence, we maintain our Buy rating on Insecticides (India) with a revised PT of Rs. 590 (reflects rollover of valuation multiple to FY2023E EPS). At CMP, the stock is trading at an attractive valuation of 7.5x its FY2022E EPS and 6.6x FY2023E EPS.

Key risk

Poor demand or a delay in launch of new products is likely to affect revenue visibility, while volatility in input costs may impact margin. The government's intention to ban 27 pesticides could impact company's performance; but the final decision is yet to come.

Valuation Rs cr

Particulars	FY19	FY20	FY21E	FY22E	FY23E
Revenues	1,194	1,363	1,404	1,573	1,698
OPM (%)	15.7	11.4	9.6	13.3	14.0
Adjusted PAT	123	87	81	135	153
y-o-y growth (%)	45.7	(29.2)	(7.1)	67.5	13.3
PAT Margin (%)	10.3	6.4	5.8	8.6	9.0
Adjusted EPS (Rs.)	59.4	42.1	39.1	65.4	74.2
P/E (x)	8.2	11.6	12.5	7.5	6.6
P/B	1.5	1.4	1.3	1.1	0.9
EV/EBITDA (x)	6.9	7.2	7.4	4.3	3.8
RoCE (%)	20.4	14.0	12.9	19.9	19.8
RoE (%)	20.3	12.5	10.6	15.7	15.3

Source: Company; Sharekhan estimates

Weak results given sharp 370 bps y-o-y contraction in OPM to 5%: Q3FY2021 revenues increased by 13.8% y-o-y to Rs. 299 crore, 11% above our estimate of Rs. 268 crore. Revenue growth was driven by a 3.7% y-o-y rise in the total branded sales to Rs206 crore, 58.4% y-o-y rise in in institutional sales while exports declined by 1.4% y-o-y. Branded sales improved due to 6.8% y-o-y growth in Maharatna sales and a 1.4% y-o-y increase in other branded sales. However, OPM witnessed 370bps contraction to 5% (306 bps lower than our estimates of 8.1%) due to a decline in gross margin by 492 bps to 21.1% (given higher raw material cost), rise in share of low margin generic products and increase in logistic cost. Consequently, operating profit was declined by 34.4% y-o-y to Rs. 15 crore, below our estimate of Rs. 22 crore. Adjusted PAT declined by 31% y-o-y to Rs. 6.1 crore, below our estimate of Rs11 crore due to weaker-than-expected margins.

Q3FY2021 conference call highlights

- **Revenues guidance –** The management has guided for revenue growth of 15% for FY2022 and of this, 12% growth would be driven by new products. The management highlighted that many new products are at 50% of their revenue potential and target will be to take it 75-80%. The company has guided for net incremental revenue of Rs. 200 crore for FY2022 (new product revenues are at Rs. 300 crore less Rs. 100 crore for Nuvan). The management has guided for flat y-o-y revenues for Q4FY2021.
- **Margin outlook –** With new product launches planned benefit of backward integration likely product price hikes, the management expects gross and EBITDA margins to gradually improve over next two years and are likely to reach at ~30% in FY2023 (versus 23.4% in 9MFY2021).
- **Focus on new product launches –** The company plans to launch 10 products in FY2021 (already launched seven new products in 9MFY2021). In Q3FY2021, the company launched two new products - Tadaaki and Avval, which contributed Rs. 5.8 crore to net sales. Of the total seven new products, Dominant and Tadaaki have received strong response from farmers. Also, management targets to Lethal Granule as a Rs. 200-crore brand.
- **Focus on reducing working capital cycle –** The company has adopted a cash & carry model to reduce receivables and reduce working capital cycles. As a result, overall cash conversion cycle has shrunk to 115 days from 184 days in FY2020. Resultantly, the company net cash stood at Rs. 35 crore as of December 2020.
- **Project update –** The management has said that development of its two manufacturing plants in Gujarat and Rajasthan is expected to get delayed by one quarter and now expect to get commissioned by June 2021. The new plants would be focused on backward integration, manufacture high value products and improve product mix in the long run. The backward integration would result in a 10-15% savings in raw material costs in certain cases and slightly higher for certain other raw materials. More importantly, access to raw material would reduce dependence upon imports and provide reliability in production.
- The management has said that Nuvan inventory was sold at discount with total sales of Rs100 crore.
- The B2C segment contributed 68.8% of overall revenues versus 75.4% in Q3FY2021, B2B accounted for 26.4% versus 18.9% of revenues and the remaining 4.9% was derived from exports.
- On-field marketing activities has picked up sharply but still it is to reach optimum level, and this would also drive sales growth going forward.

Results Rs cr

Particulars	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ(%)
Revenue	**299.2**	**262.9**	**13.8**	**455.8**	**(34.4)**
Operating profit	15.1	23.0	(34.4)	57.7	(73.9)
Other Income	1.0	0.8	33.1	5.0	(79.6)
Depreciation	6.2	6.1	1.8	6.2	(0.1)
Finance Cost	1.9	6.2	(69.8)	1.4	32.4
PBT	8.2	11.8	(30.4)	55.4	(85.2)
Tax	2.1	2.9	(28.7)	13.8	(85.1)
Reported PAT	6.1	8.9	(30.9)	41.6	(85.2)
Adjusted PAT	**6.1**	**8.9**	**(30.9)**	**41.6**	**(85.2)**
Reported EPS (Rs)	3.0	4.3	(30.9)	20.1	(85.2)
Margins (%)	**Q3FY21**	**Q3FY20**	**YoY (BPS)**	**Q2FY21**	**QoQ(BPS)**
OPM (%)	5.0	8.7	(370)	12.7	(763)
Adj. NPM (%)	2.1	3.4	(133)	9.1	(707)

Source: Company; Sharekhan Research

Revenue mix by segments Rs cr

Revenues by segment	Q3FY21	Q3FY20	y-o-y (%)	Q2FY21	q-o-q (%)
B2C	206	198	3.7%	335	-38.7%
BCB	79	50	58.4%	107	-26.1%
Exports	15	15	-1.4%	14	5.8%
Total revenues	**299**	**263**	**13.8%**	**456**	**-34.4%**
Revenue mix (%)	**Q3FY21**	**Q3FY20**	**y-o-y (bps)**	**Q2FY21**	**q-o-q (bps)**
B2C	68.8	75.4	-668	73.6	-481
BCB	26.4	18.9	743	23.4	296
Exports	4.9	5.6	-75	3.0	185

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Rising food demand provides ample growth opportunities for agri-input players

The outlook for the Indian agrochemical industry is encouraging, primarily driven by rising foodgrain production and domestic demand, favourable regulatory reforms for farmers (government passed key agri-sector reforms namely Farmers Produce Trade and Commerce Bill 2020 and Farmers (Empowerment & Protection) Agreement of Price Assurance & Farm Services Bill). Moreover, there is a vast opportunity from products going off-patent. The government's focus is to double farmers' income (higher MSPs for crops); near-normal monsoons and higher reservoir levels would augment demand for agri-input in India. We also expect exports from India to grow at a strong pace as India is being looked as the preferred supplier for agri-input products given supply disruption from China. Thus, we expect India's agrochemical industry to witness a 7-8% growth annually on sustained basis over the next few years.

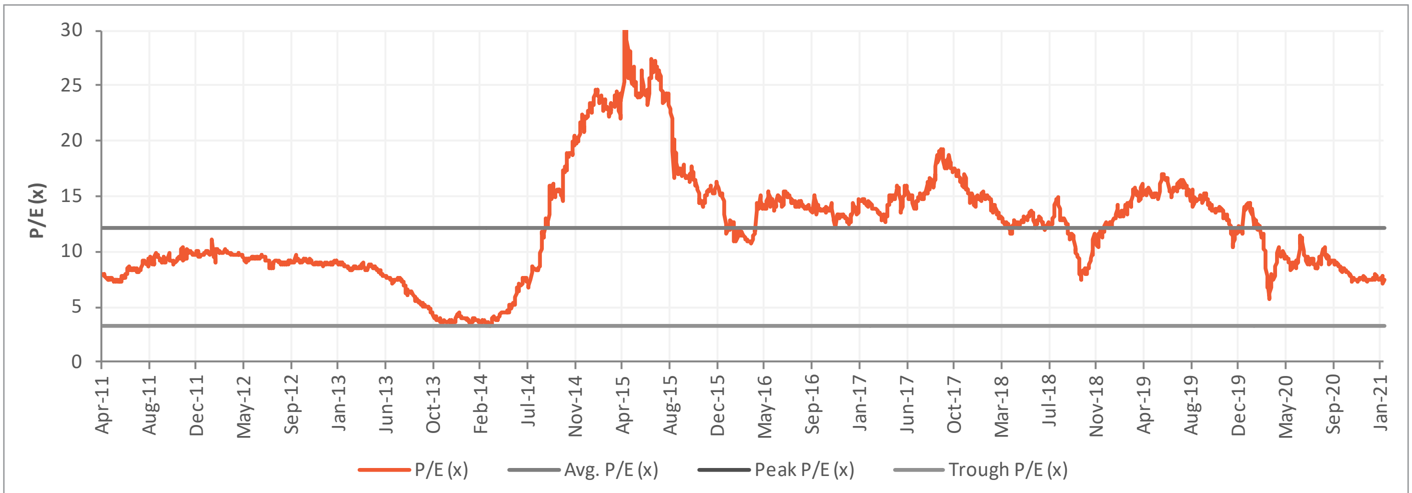
■ Company Outlook – New product launches and capex to drive performance

A healthy monsoon has been driving demand during the Kharif season and increased water levels in reservoir are setting the tone for a good Rabi season too. The management expects a healthy growth overall backed by increased business from branded products, institutional sales and higher exports. The same is expected to be achieved through a focus on launching innovative products, a better product mix to deliver sustainable growth, and enhanced profitability going forward. The management has guided for a 15% revenue growth for FY2022E.

■ Valuation – Maintain Buy on Insecticides (India) with a revised PT of Rs. 590

We have lowered our FY2021 earnings estimate to factor in a weaker-than-expected margin performance in Q3FY2021 and have fine-tuned our FY2022-FY2023 earnings estimates. We believe that revenue growth momentum would pick up with a ramp-up in revenue contribution from new products, while backward integration and potential increase in product prices price would take gross margins back to historical level of ~29-30% by FY2023E. We thus expect strong revenue, EBITDA and PAT CAGR of 10%/33%/38% over FY2021E-FY2023E (owing to low base in FY2021 due to COVID-19) along with a decent RoE of 15-16%. Hence, we maintain our Buy rating on Insecticides (India) with a revised PT of Rs. 590 (reflects rollover of valuation multiple to FY2023E EPS). At CMP, the stock is trading at an attractive valuation of 7.5x its FY2022E EPS and 6.6x FY2023E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

IIL is India's leading and one of the fast-growing agrochemical companies. The company has emerged as a frontline performer in India's crop care market and is all set to grow impressively. The company has more than 100+ formulation products and 22 technical products and manufactures all types of insecticides, weedicides, fungicides, and PGRs for all types of crops and households. The company owns the prestigious Tractorbrand, which is highly popular among farmers. This umbrella brand of its agro products, such as Lethal, Victor, Monocil, Xplode, Hijack, Pulsor, and Hakama, signifies IIL's deep connection with farmers. The company has five state-of-the-art formulation facilities in Chopanki (Rajasthan), Samba and Udhampur (Jammu & Kashmir), and Dahej (Gujarat). The company also has two technical synthesis plants at Chopanki and Dahej to manufacture technical-grade chemicals, providing a competitive edge by backward integration. The company also has a bio manufacturing unit and four dedicated research facilities. The company markets its products through more than 60,000 retail outlets with the help of 3,000 distributors and 31 depots/branches having sales team of over 500 personnel.

Investment theme

Strategic transition yielding results: IIL's management took strategic steps towards realigning the product mix by introducing NewGen products through higher R&D thrust and weeding out the old generic products for more sustainable growth visibility with improved margin trajectory. The transition has started yielding results, with strong new launches and improved margins.

Four growth pillars driving performance: IIL's management has chalked out a four-prolonged strategy for long-term sustainable growth acceleration with new product launches – (1) reverse engineering; (2) combination products; (3) biological products; and (4) product discovery.

Key Risks

- Poor demand offtake or delay in the launch of new products is likely to affect revenue visibility, while volatility in input cost may impact margin profile.
- The government's intention to ban 27 pesticides could have an adverse impact on the company's performance; however, the final decision is yet to come.

Additional Data

Key management personnel

Hari Chand Aggarwal	Chairman
Rajesh Aggarwal	Managing Director
Nikunj Aggarwal	Whole Time Director
Sandeep Aggarwal	Chief Financial Officer
Sandeep Kumar	Company Secretary & Compliance office

Source: Company Website

Top shareholders

Sr. No.	Holder Name	Holding (%)
1	HDFC Asset Management Company Ltd	8.4
2	Life Insurance Corp of India	1.5
3	FMR LLC	1.5
4	BNP Paribas Asset Management India	1.0

Source: Bloomberg

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Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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