Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

PI Industries Ltd

Strong Q2; growth guidance healthy

Agri Chem		Sharekhan code: PIIND		
Reco/View: Buy	↔	CMP: Rs. 3,641	Price Target: Rs. 4,500	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Q2 results were strong with a 44% y-o-y growth in PAT to Rs. 481 crore (10% beat) led by robust growth in CSM, margin expansion of 165 bps (despite one-offs and pharma overheads), lower tax rate.
- CSM revenue (Agri-chem exports) growth of 22% y-o-y was robust, led by higher volumes, but domestic revenues declined 2% y-o-y due to delayed/erratic monsoon. Apart from agrochem molecules, the growth was also supported by electronics and specialty chemicals.
- Healthy FY24 revenue guidance (ex-pharma) of 18-20%, which would be led by volume growth and expects margin improvement. Post integration, pharma business margin expected to 20-22%.
- We maintain our Buy rating on PI Industries with a unchanged PT of Rs. 4,500. Pharma foray to diversify earnings stream and drive meaningful medium to long-term earnings growth; surplus cash of Rs. 2,891 crore to help pursue organic/inorganic growth opportunities. The stock trades at 26x its FY2026E EPS.

Q2FY24 results were decent with consolidated revenue of Rs. 2,117 crore (up 19.6% y-o-y) was in line with our revenue estimate. The strong growth was led robust 22% y-o-y growth in CSM exports (excluding Pharma) revenue, driven by volume growth of ~21% y-o-y and ~1% from price, currency, and favourable product mix. However, domestic revenue declined by 1.6% y-o-y to 484 crore due to delayed and erratic spread of monsoon. OPM improved by 165 bps y-o-y to 26.0% and was 102 bps higher than our estimate of 25.0% mainly due to higher gross margin and better product mix. The beat in margin was despite provision of Rs. 40 crore for loss of material due to theft and higher development cost for pharma business. Consequently, operating profit grew by 27.7% y-o-y to Rs. 551 crore (in line with our estimate). PAT at Rs. 481 crore (up 44% y-o-y) was also 10% above our estimates of Rs. 438 crore due to lower effective tax rate of 6.2% (versus assumption of 13.4%).

Key positives

- Strong revenue growth of 22% y-o-y in CSM business mainly led by volume growth.
- Beat of 102 bps in OPM at 26.0% due to 135 bps beat in gross margins.

Key negatives

- Domestic revenue fell by 2% y-o-y due to erratic spread of monsoon.

Management Commentary

- Revenue growth (ex-pharma) guidance of 18-20% for FY24 and expects continued margin improvement.
- Pharma revenue/EBITDA/PAT of Rs. 72 crore/-18 crore due to IND-AS impact; expect positive contribution in H2FY24. Gradually expect pharma business margins to reach 20-22%. Integration of CRO-CDMO-API platform underway for pharma. x
- Capex plan of Rs. 800 crore versus H1FY24 capex of Rs. 266 crore in H1FY24. Capacity expansion for CSM.
- Plan to commercialise 4-5 products every year for CSM. H1FY24 – Commercialised 3 new products in CSM and 4 in domestic agri brands.
- Overall, inventory destocking is gradually improving; Brazil has major challenges given high stocking in previous year.

Revision in estimates – We have fine-tuned our FY23-25 earnings estimate. We have introduced our FY26 earnings estimate in this report.

Our Call

Valuation – Maintain Buy on PI with an unchanged PT of Rs. 4,500: PI's pharma foray would diversify its earnings stream and drive medium to long-term growth for the company. Even post recent acquisitions, PI would have a strong net cash position of Rs. 2,891 crore to pursue both organic and inorganic growth opportunities. We expect PI's revenue/EBITDA/PAT to post a strong CAGR of 19%/20%/21% over FY2023-FY2026E, led by robust CSM order book of $1.8 billion, ramp-up of nine new products commercialised in the last one year and launch of new products in FY2024. Growth would further improve post integration of pharma segment. We maintain a Buy rating on PI with an unchanged PT of Rs. 4,500. At the CMP, the stock trades at 29.7x its FY2025E EPS and 25.7x its FY2026E EPS.

Key Risks

1) Delay in the commissioning of projects or execution of orders or delayed orders by clients in the export business can affect revenue growth and 2) higher-than-normal time lag in passing on the increase in raw-material prices could affect margins.

Valuation (Consolidated) Rs cr

Particulars	FY23	FY24E	FY25E	FY26E
Revenue	6,492	7,818	9,281	10,966
Growth (%)	22.5	20.4	18.7	18.2
EBIDTA	1,701	2,047	2,473	2,947
OPM (%)	23.8	24.2	24.6	24.9
Adjusted PAT	1,223	1,574	1,869	2,162
y-o-y growth (%)	45.5	28.7	18.7	15.7
Adjusted EPS (Rs.)	80.0	103.1	122.5	141.8
P/E (x)	45.5	35.3	29.7	25.7
EV/EBITDA (x)	33.8	27.3	22.2	18.1
P/BV (x)	7.7	6.3	5.3	4.4
RoCE (%)	21.3	22.4	22.5	22.5
RoE (%)	18.3	19.7	19.3	18.6

Source: Company; Sharekhan estimates

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 34.41

Updated Aug 08, 2023

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

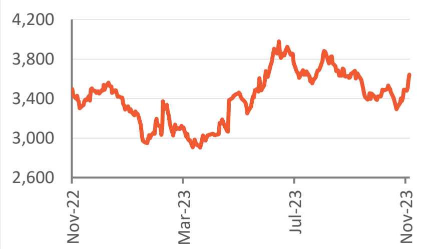
Company details

Market cap:	Rs. 55,244 cr
52-week high/low:	Rs. 4,010 / 2,870
NSE volume: (No of shares)	3.0 lakh
BSE code:	523642
NSE code:	PIIND
Free float: (No of shares)	8.2 cr

Shareholding (%)

Promoters	46
FII	20
DII	23
Others	11

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5	-6	6	4
Relative to Sensex	7	-5	1	-3

Sharekhan Research, Bloomberg

Stock Update

Result Update

Q2FY24 conference call highlights

- **Operating scenario:** Erratic monsoons forced farmers to hold back on application of crop protection products. China induced continuously falling prices of raw materials are putting pressure on the selling prices of generic portfolio. Similar scenarios exist in global market where prices are also under pressure, channel inventory is high and distributors (US& Brazil) are prioritizing destocking and filling up the requirement for the lower-priced stocks.
- **Company Growth Outlook:** While industry is facing headwind due to an adverse operating scenario, PI has reported growth of 22% over the last quarter mainly due to different operating model, which based on differentiated IP-based products and niche capabilities. Company's pipeline of molecules diversified across multiple end users' industries. Due to the healthy molecules pipeline, the company expects high growth in the future.
- **Guidance:** Management expects to maintain growth guidance of 18-20%, with the expectation of further growth in H2FY24 and eyes continued improvement in margins.
- **Transit Losses:** Company lost a few containers due to theft valued at Rs. 40 crores. Though the material has been recovered the case is still under investigation. Taking a conservative approach, management accounted for the material loss in the financial statement for this quarter.
- **Margin Improvement:** Favorable revenue mix rather than changing volume and value which led to improvement in overall margins.
- **Inventory destocking:** As consumption is strong in different geographies, hence the situation related to inventory destocking is improving. Management believes that in the next few quarters channel inventory should normalize.
- **Pharma business:** Post integration, the management will be able to ramp up production and expects to reach a margin of 20-22%.
- **Others** 1) CSM Exports Order Book - $~1.8 billion 2) Company commercialized 3 new products in Exports and 4 in Domestic Agri Brands 3) The company has guided Rs. 800 crore capex for the year.

Results (Consolidated) Rs cr

Particulars	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)
Net Sales	**2,117**	**1,770**	**19.6**	**1,910**	**10.8**
Total expenditure	1,566	1,338	17.0	1,443	8.5
Operating profit	**551**	**432**	**27.7**	**468**	**17.9**
Other Income	47	32	47.9	47	-
Depreciation	80	56	43.4	70	15.2
Interest	8	11	(29.7)	4	81.4
PBT	**510**	**397**	**28.7**	**441**	**15.8**
Tax	32	63	(49.6)	63	(49.3)
RPAT	**481**	**335**	**43.5**	**383**	**25.5**
EPS (Rs.)	31.6	22.0	43.5	25.2	25.5
Margin (%)			**YoY (BPS)**		**QoQ (BPS)**
Gross profit margin	46.6	45.2	135	46.5	5
Operating profit margin	26.0	24.4	165	24.5	156
Net profit margin	22.7	18.9	378	20.0	266

Source: Company; Sharekhan Research

Revenue break-up Rs cr

Particulars	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)
Domestic	484	492	-1.6	347	39.3
Exports	1,633	1,278	27.7	1,563	4.5
Total revenues	**2,117**	**1,770**	**19.6**	**1,910**	**10.8**

Source: Company; Sharekhan Research

Targeting to achieve 18%-20% revenue growth in FY24 with continued improvement in margins and returns

Domestic:
Focus on portfolio diversification with high quality revenue

- Monsoon deficit in south and low reservoir levels
- Elevated inventory levels in the industry for row crop agchem products and price pressure from generics
- Focused to support farmers with a crop solution approach and new brand launches
- Expecting recovery in niche crop segments

CSM Export:
Technology focused approach to drive incremental business

- Continued scale up in demand of the existing and newly commercialised products
- Solid R&D pipeline of diversified portfolio of agchem, electronic, imaging and other specialty chemicals - 4 to 5 products to be commercialized every year
- Capacity expansion in line with plan
- Momentum in new enquiries and conversion to continue

Health Science:
Building a differentiated play in Pharma CDMO space

- Build-up of Hyderabad research center and staffing at full swing
- Operating model, functional and IT integration of acquired companies (Archimica, Therachem Medilab) underway
- Working with global advisors for business transformation across Commercial, R&D, Manufacturing, Supply Chain
- Capex committed for upgrade of facilities and building cutting-edge capabilities

Progressing on strategic initiatives in line with plan

- Strong pipeline of Biologicals and Biostimulant products at different stages of development
- Working on new technologies and building blocks for future growth
- Discussions continues with global innovators for development partnership of promising R&D leads
- Evaluation of opportunities for inorganic growth continues in multiple strategic areas

Source: Sharekhan Research

Outlook and Valuation

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

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 the Farmers Produce Trade and Commerce Bill 2020 and Farmers (Empowerment & Protection) Agreement of Price Assurance & Farm Services Bill) and the vast opportunity from products going off-patent. The government's focus is to double farmers' incomes (higher MSPs for crops); near-normal monsoon and higher reservoir levels would augment demand for agri inputs in India. We also expect exports from India to grow at strongly as the country is being looked as the preferred supplier for agri inputs given supply disruption from China. Thus, we expect India's agrochemicals industry to grow by 7-8% annually on a sustained basis for the next few years.

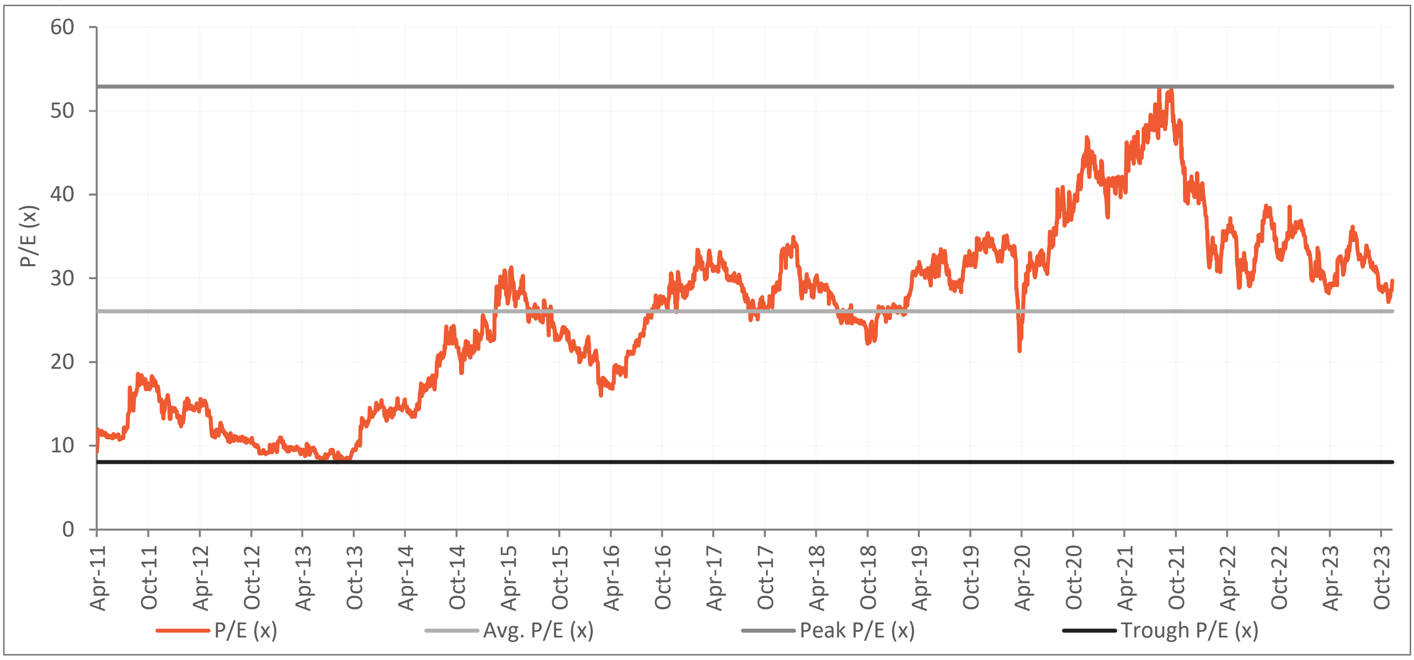
■ Company Outlook – Strong growth outlook led by organic and inorganic opportunities:

Demand remains encouraging in both domestic (strong Rabi season outlook) and export markets (order book of $1.8 billion) and the company has guided for 20% revenue growth and margin improvement for FY2023. Commissioning of additional capacity and contribution from newly-launched brands would fuel growth. Moreover, utilization of some portion of QIP money for recently announced pharma acquisition would drive inorganic growth over the medium to long term, apart from diversifying its business and enhancement of technological capabilities.

■ Valuation – Maintain Buy on PI with an unchanged PT of Rs. 4,500

PI's pharma foray would diversify its earnings stream and drive medium to long-term growth for the company. Even post recent acquisitions, PI would have a strong net cash position of Rs. 2,891 crore to pursue both organic and inorganic growth opportunities. We expect PI's revenue/EBITDA/PAT to post a strong CAGR of 19%/20%/21% over FY2023-FY2026E, led by robust CSM order book of $1.8 billion, ramp-up of nine new products commercialised in the last one year and launch of new products in FY2024. Growth would further improve post integration of pharma segment. We maintain a Buy rating on PI with an unchanged PT of Rs. 4,500. At the CMP, the stock trades at 29.7x its FY2025E EPS and 25.7x its FY2026E EPS.

One-year forward P/E (x) band



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 fifteen multi-product plants under its four 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 500 scientists and researchers.

Investment theme

A strong CSM order book of ~$1.8 billion and decent growth in domestic formulation business provides strong long term revenue growth visibility. The company has organic and inorganic growth aspirations in areas such as enhancement of technological capability, de-risking manufacturing concentration in India. The recent pharma acquisition would accelerate earnings growth prospects for the company.

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 increased raw-material prices could affect margins.
- Delay in utilisation of QIP money.

Additional Data

Key management personnel

Narayan K. Seshadri	Non-Executive & Independent Chairperson
Dr. Raman Ramachandran	Managing Director & Chief Executive Officer
Mayank Singhal	Vice Chairman and Managing Director
Rajnish Sarna	Executive Director
Arvind Singhal	Non-Executive - Non Independent Director
Manikantan Viswanathan	Chief Financial Officer
Naresh Kapoor	Company Secretary & Compliance officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Axis Asset Management Co Ltd/India	5.68
2	BlackRock Inc	2.28
3	Vanguard Group Inc/The	2.12
4	Kotak Mahindra Asset Management Co	2.11
5	Life Insurance Corp of India	1.86
6	UTI Asset Management Co Ltd	1.41
7	Canara Robeco Asset Management Co	1.35
8	ICICI Prudential Life Insurance Co	1.09
9	ICICI Prudential Asset Management	1.05
10	Capital Group Cos Inc/The	0.92

Source: Bloomberg

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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