Inspired by Science

PI Industries Ltd

BSE: 523642 | NSE: PIIND | ISIN: INE603J01030

SECTOR: PESTICIDES & AGRO CHEMICALS

Current Price	**₹ 863**
Target Price	**₹ 1006**
Recommendation	**BUY**
Upside	**17%**

Market Cap (₹) 119.8 Billion	**P/E** 37.7
6M Average Volume 125,769	**P/B**: 10.2
52-Week Range 497.55 - 892.30	**Dividend Yield** 0.36%
TTM EPS 28.79	**Book Value** 101.58

Annual Ratios (%)

	1-Year	3-Years	5-Years
Growth			
Revenue	9.01	22.40	23.62
Net Profit	28.24	47.96	37.10
EPS	27.72	47.36	31.63
Book Value	30.18	29.77	36.21
Average			
Operating Margin	20.64	19.32	17.79
Net Margin	13.59	11.89	10.84
RONW	30.54	30.78	30.91
ROI	35.75	37.07	33.83

SHARE HOLDING PATTERN (%)

	Current	Q3FY16	Q2FY16
Promoters	51.7	51.7	58.4
MF's, FI's, BKs	13.6	13.1	8.8
FIIs	20.6	20.5	17
Others	14.1	14.7	15.9

*** Promoters pledged shares (% of share in issue): NIL**

Key Drivers

PI boasts of a unique business model—a strong R&D -led custom synthesis business (60% of revenues), and an equally compelling domestic agro -chemicals business (40% of revenues), largely built by in–licensing arrangements with major global agro-chemicals innovators.

CSM Exports Robust Growth in FY17-With a strong order book amounting to USD850m, the CSM business has robustrevenue visibility; we thus expect 20% revenue CAGR over FY16-18.

Good Monsoons: Domestic Agri input outlook is improved on account of better monsoons with increase rural consumption.

Strong Product Line: With a mere 10% penetration, we believe there is untapped growth potential in PI's largest product—**Nominee Gold**, which (along with new products like **Sheen, Vibrant**) will continue to drive growth momentum for the domestic agro-chemicals business.

Outlook & Valuations: With best-in-class capital efficiency **35.75%** RoCE, debt-free balance sheet, robust growth outlook—**23%** revenue CAGR and **37% PAT** CAGR over the 5 years).

Potential Growth in generic products owing to the expiry of patents in the FY 17 worth of 1.7Bn.

We believe PI is one of the best plays on India's agri-sector and CSM opportunities.

Shortlisting Methodology

Indian market has close to 8000 companies listed as part of National Stock Exchange (NSE) and Bombay Stock Exchange (BSE) out of the total 38729 registered companies. We shortlisted the 5 companies following the below methodology.

- **Step 1:**We took the entire super set of the companies listed in India on the major stock exchanges NSE and BSE.The count of listed companies including dormant/closed companies was **7836**.(Source- Prowess Dx: http://prowessdx.cmie.com/)

- **Step 2:** Then we filtered out the companies for which we did not have sufficient data for the last 5 years and that have not traded actively, bringing down the list to about **1946** companies. The rationale behind this step is that we strongly believe that we need at least 5-year history of the company to perform valuation of the company.

- **Step 3:** Further, we apply the criteria of **Piotroski 'F Score'** (9 points)and **Internal Growth Indicator score** (11 points)– which provides a composite score of recent financial health of the firm.

  Internal Growth Indicator Score of 11 points was based on the following criteria:

CAGR of PAT > 20%	3 points
CAGR of Revenue > 20%	1 point
No negative growth in PAT for last 5 years	1 point
No negative growth in Revenue for last 5 years	1 point
Minimum PAT margin of 7% in last 5 years	2 points
Minimum RONW of 10%	1 point
Minimum ROCE of 10%	1 point

  *Companies obtaining a score of minimum 16 out of 20points gave us a list of**24**potential companies*.

- **Step 4:** Out of the above 24 companies that were zeroed down to, furtheranalysed the market valuation to see how the market has priced them. We picked up the **5** stocks with a strong intrinsic value, from the diversified sectors, and solid potential to grow over the next few months and years.

- **Step 5:**Of the 5 stocks we further researched and identified **PI Industries Ltd** as our top pick to pitch, PI, an Agro Chemical company, has over the last 65 odd years consistentlyperform good business in comparison to peers. Good fundamentals, strong future line up of products, sticky high margin revenue and positivemacro factors are working in the favour of PI Industries Ltd.

The India Story

Indian economy is on the verge of paradigm shift. The key enablers are stable annual economic growth rate on the back of strong reforms initiated by Government, lower inflation, rising foreign exchange reserves and booming capital markets amongst others. India also ranked highest in terms of consumer confidence during all 4 quarter of the financial year 2015-16 (FY16) as per the global consumer confidence index created by Nielsen. *India's gross domestic product (GDP) grew 7.6% in FY16, which reinforces India's position as the world's fastest growing large economy and according to IMF Economic Outlook Indian economy will continue to grow more than 7% in FY17.*

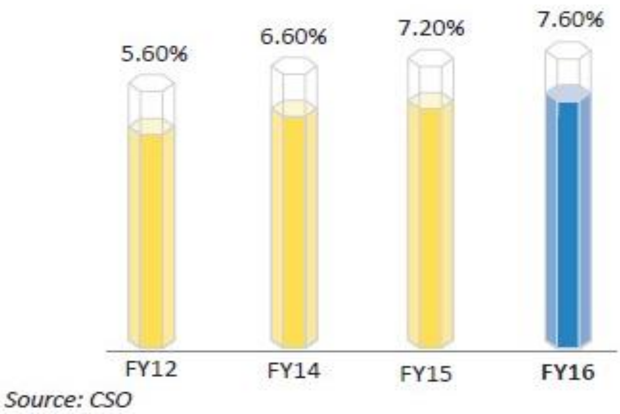

Figure 1: Indian GDP growth rate (Base year 2011-12)

Owing to the various policy and budgetary measures aimed at rebooting the country's economy to a higher growth trajectory coupled with resolute persuasion of reforms by the Central Government, economic activities are steadily reviving. While the revival of consumer confidence is getting reflected in the handsome growth in sales of passenger cars, the effect of increased public spending on high ticket infrastructure, railway and defence projects shall aid to restart a moderate pick up in private investments in the manufacturing sector. *The forecast of good monsoon on the back of the increased rural thrust of the union budget 2016 shall help strengthen the rural activities and consumption cycle. Implementation of the 7th Pay Commission recommendations and OROP scheme shall boost retail consumption*.

Soil Health Card Scheme is a scheme launched by the Government of India in February 2015.The scheme aims at promoting soil test based and balanced use of fertilizers to enable farmers realize higher yields at lower cost.**Crop Insurance Scheme** launched by Government of India in Jan 206. The main motto is to provide a more efficient insurance support to the farmers of the country and become a financial support to thousands of farmers. **Direct Benefit Transfer for Fertilizers** is successfully implemented on the Pilot basis and will be roll out to all the states in India. This scheme is going to benefit the farmers and Agro manufacturers.

Further reduction in retail cost of borrowing, likely to be pursued in light of contained inflation, augurs well. Due to the continued thrust of impending high impact economic reforms such as the GST, land, labour, etc., the Indian economy appears set to shift to 8-9% growth range in the coming years.

Agro Chemical Industry Overview

Agrochemicals namely fertilizers, pesticides, hormones and plant growth regulators play an important role to enhance plant and soil health, improve farm yields and farming income. Global market for agrochemicals stood at $207bn in calendar year 2014 and will grow at a CAGR of 3.2% to reach $250.5bn by 2020.Major drivers for the industry is the shrinking farmland coupled with increase in Global population make it inevitable but extract more yield per hectare, thereby increasing demand for agrochemicals.

India Agro Chemical Industry:

The Indian agrochemicals is estimated to grow by 12% every year to reach 7.5 billion by FY19 with export contributing about 50%.Agro chemical sector business prospects are dependent on agriculture and more than 60% of India's agriculture is still monsoon dependent. Financial year '15 and '16 had a bad monsoon which resulted in low demand for agrochemical products.Indian agrochemicals prospects look bright for FY'17 on the back of above average monsoon prediction by Indian Meteorological Department.

Industry Growth Drivers:

1) Increased demand for food grains
2) Low consumption level (India has the lowest pesticide consumption)
3) Sustained government support
4) Wastage of Agri output& Low farm productivity

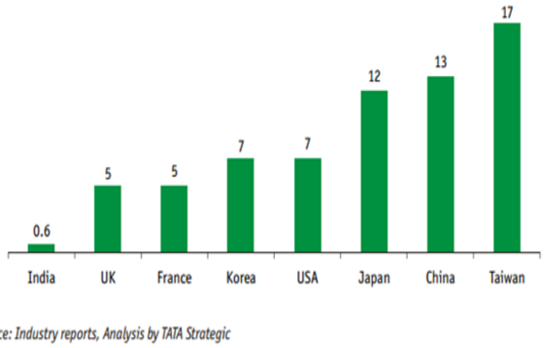

Figure 2: Pesticide consumption (Kg/ha) comparison (FY 15)

Future export growth prospects:

Agrochemicals worth USD 4.1 billion are expected to go off-patent by 2020. This provides significant export opportunities for Indian companies which have expertise in generic segment. Companies could also look for strategic alliances with local companies to expand their marketing and distribution reach. Merger and acquisition opportunities could also be explored to increase their global presence.

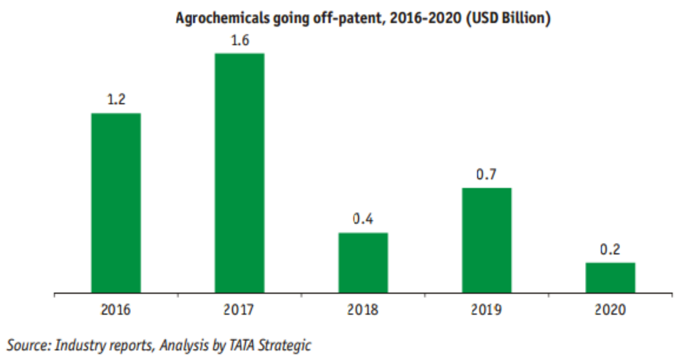

Figure 3: Growth opportunities in Generic Products

Challenges for industry:

1) Heavy dependence on Monsoon
2) High R&D costs

3) Low awareness of agrochemicals and using them judiciously
4) Threat from Genetically Modified seeds, as they possess self-immunity - impact the business of agrochemicals.

PI Industries Ltd

Incorporated in 1947, PI Industries Limited is an Agri Input & Custom Synthesis & Manufacturing company in India. Employee strength of 18000.

Recognitions:

1) PI Industries won the Golden Peacock Award for Quality in the year 2016. held at Hotel- The Meydan, Dubai (UAE) on 20th April 2016.
2) PI Industries CMD, Mr.Salil Singhal yet again awarded India's Best CEO in 2015.
3) PI industries wins the Golden Peacock Environment Management Award 2015 at the 17th World Environment Congress, organized by Institute of Directors presented by Prakash Javadekar, Honourable Union Minister of State for Environment.
4) PI Industries, IT Team receives award on DQ Business Tech, Business Impact and Innovative CIO Award 2015

Business Principle - Integrated Entity with a non-compete approach driven by respect for intellectual property.

a) **Domestic Agri Inputs** - offering plant protection products, and specialty plant nutrient products and solutions. PI has a strong rural reach and brand equity, with millions of Indian farmers duly backed by a robust pipeline of products for sustained growth in the sector.

PI is a complete agro-chemicals player as it provides protection across crop categories. Insecticides contribute ~50% to revenues, followed by herbicides (~30%) and fungicides (~20%). PI's top eight products include Nominee Gold, Keefun, Biovita X, Foratox, Osheen, Melsa, Vibrant and Carina.

PI has managed to have exclusive tie-ups with patent originators, led by its track record of respecting innovators' IPR. The company's focus on selected and patented innovative products through in-licensing differentiates it from the rest of the market participants who sell largely generic products with little product differentiation.

PI currently has a product portfolio spanning 35 brands across categories (herbicides, insecticides, fungicides and specialty chemicals), including 5 -6 products that are in-licensed and 10 -12 products that are co-marketed. With higher proportion of in-licensed and co-

marketing revenues as against generic products, PI enjoys industry-leading margins in the domestic agro-chemicals division.
Strategy: Tradition of introducing 1 – 2 new products every year leading to sustained revenue growth and healthy margins.

- Vibrant (Insecticide)
- Biovita X (Plant Nutrient)
- Legacee (Herbicide)

Strong product portfolio—35 brands across categories

Category	Brands
Insecticides	Osheen, Oval, PI Bupro, Lepido, Dodger, Colt, Divap, Colfos, Fosmite, Fluton, Jumbo, Snailkil, Foratox, Roket, Carina, Simbaa, Voltage, Maxima,Vibrant
Herbicides	Nominee Gold. Bunker, Melsa, Solaro, PI Glypho, INRO, Bingo, Pimix,
Fungicides	Cuprina, Lurit, Kitazin, Sanipeb, Clutch, Logik
Specialty chemicals	Biovita ,Biovita X

Source: Company, MOSL

b) **Custom Synthesis & Manufacturing (CSM)** - for contract research and production of agro-chemicals, intermediates and other niche fine chemicals for global innovators. The business, backed with a strong R&D support, works to develop and commercialize products based on newly discovered chemistries with reputed MNC innovators.

IPR protection is vital criteria for global innovators to choose partners in the CSM business and all Indian players are subject to TRIPS agreement, which provides IPR protection. Additionally, economic competencies relative to China have also gradually improved over the last few years. These factors make Indian players an economically viable choice.

PI has exhibited strong scale-up and execution capabilities in CSM, which involves complex activities, and has accreditation for GLP along with best-in-class support infrastructure; this has led to longstanding relationship with global innovators in the agro -chemical space and acts as major entry barrier for new entrants.

PI participates in early stage of molecule life cycle, which enables it to participate in the growth phase of products. The company's robust order book of USD850m provides revenue visibility over the next two years and will be complemented by facilities in Jambusar.

- R&D spend Increase 50% YOY. R&D Capital Expenditure: Company has completed first phase of the expansion of R&D set up by constructing one floor of two-story building planned of approx. 60,000 square feet containing "state-of-the-art" process synthesis and analysis laboratory Equipped with R&D Facilities, accredited for GLP and 'Norms on OECD Principles' by (NGCMA), in Udaipur.

- Multi Locational Manufacturing facilities

- 5 Multi-purpose plants and 3 Formulation units at Panoli spread over 79000 sq m.
- 3 multi-purpose plants set up in Jambusar has added the capacity to meet with the increased demand from our global customers.
- The new plants in Jambusar will have a 10-year tax break (first 5 years 100% and subsequent 5 years 50% tax exemption) on all products manufactured. We expect these plants to contribute majorly to the revenue going ahead, leading to margin expansion and tax savings.

Manufacturing facilities are ISO 9001, ISO 14001, OHSAS 18001 and ISO 17025 certified.

- Developed Brand Recognition & Pan-India presence through a vast distribution network with over 10,000 distributors.

- Implementation of in-memory Database 'SAP HANA' enabled real time tracking of account, billing and material improvement. This resulted in optimization of working capital Management.

- Leveraging its expertise in complete chemistry, PI planned to foray in to the Pharma sector for manufacturing and export of early intermediates.

Key growth drivers

- Growing food demand with limited land availability will lead to higher focus on crop yields. Escalating labor costs are driving demand for herbicide s (as against manual weed cutting), thus ensuring higher agrochemicals usage. India's pesticide consumption (0.75 Kgs/Ha) is amongst the lowest globally

- Strong export opportunity: Low-cost manufacturing, availability of technically skilled manpower, seasonal domestic demand, available capacity, better price realization globally and strong presence in generic pesticide manufacturing.

- Agro-chemicals worth USD4.1b are expected to be off patent by 2020; this presents a large opportunity for Indian companies such as PI Industries to participate in the global generics business

Valuation

We are projecting a target price of INR 1006 from the current market price of INR 863(as on 28-Oct-2016) on NSE, giving the stock an upside of 17% in 12-month period. For Discounted cash flow we have arrived at Weighted Average Cost of Capital(WACC) of 13.02%. For WACC, we calculated Cost of Equity (COE) using the Risk Free Market rate(R_f) of 6.81% which is the current prevalent 10-year government bond rate and Market return rate (R_m) of 16.2%, which is the 36-year return of the SENSEX index. Beta value is 0.63 considering 1 year of market volatility (as per Economic Times). Cost of Debt is taken as 10% which is the interest rate for '**AA**' Crisil Credit Rated companies. Debt/Equity ratio for PI Industries stands at 0.13 as of Mar 2016. India being predominantly agrarian economy with agriculture being the major contributor to the national GDP, we assume the agrochemical industry like PI Industries to grow with a terminal/horizon growth rate of 6%.

DCF Summary:

Particulars	Amount (INR mn.)
WACC	12.37%
COE	13.47%
Beta	0.63
D/E Ratio	0.13
Cost of Debt	10%
Total DCF for 10 years	44,064
Discounted Terminal value*	93,834
Total Value	1,37,898
Number of shares (in millions)	137
Value per share (INR)	1,006

PEER Comparison

PI Industries has the highest ROCE 34.96 .Higher ROCE indicates company is effectively utilising the Capital Employed to generate better returns in comparison to its peers.

PI Industries has low Dividend Yield 0.36 because PI industries is heavily investing their profits in Capex. (New Plants set up in in Jambasur and R&D facility expansion in Udaipur)

PI Industries P/E & P/B ratio clearly reflects investor confidence in the Company's expansion and diversification (Intermediaries pharma) strategy.

Particulars	PI Industries	Bayer CropScien	Rallis India	Monsanto India
Enterprise value (EV)	1,19,214.08	1,42,726.53	39,847.04	38,775.37
Enterprise value to EBIDTA (EV/EBIDTA)	25.52	28.84	18.82	32.54
Price to Earnings (PE)	37.79	50.10	33.90	39.92
Price to Book (PB)	10.25	8.59	4.94	9.78
Dividend Yield	0.36	0.40	1.13	-1.28
ROCE	34.96	24.01	20.44	26.72

DCF valuation indicates that stock can move upside 17 %. PEER comparison also reveals there is a momentum for PI industries. This certifies that PI industry is 100% buy on Market Sentimeter.

Annexure I

Free cash flow projection for 10 years as per the valuation model provided in “The Warren Buffet Way”.

Particulars	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24	FY25	FY26
	Actual	Projected	Projected	Projected	Projected	Projected	Projected	Projected	Projected	Projected	Projected
Cash flow from operations	3,527	4,179	4,953	5,869	6,955	8,241	9,766	11,573	13,714	16,251	19,257
Capex	-3,214	-2,500	-1,000	-500	-500	-1,500	-1,000	-500	-500	-500	-750
Free cash flow	313	1,679	3,953	5,369	6,455	6,741	8,766	11,073	13,214	15,751	18,507
Discounted Cash flow (DCF)		1,495	3,130	3,784	4,048	3,763	4,354	4,894	5,198	5,514	5,765

Particulars	Amount (INR mn.)
Total DCF for 10 years	41,945
Discounted Terminal value*	95,940
Total Value	1,37,885
Number of shares (in millions)	137
Value per share (INR)	1,006

*Perpetual growth rate assumed at 6%

4 ADDITIONAL INVESTMENT IDEAS

KPIT Technologies

KPIT Technologies is a MNC headquartered in Pune that provides product engineering services and solutions, IT consulting services and technologies to its clients. Mainly focused on three industries namely manufacturing, automotive & transportation and energy & utilities, with clients such as Cummins, Paccar, Lafarge etc.
In the automotive domain, KPIT has recently created a well known solutions name REVOLO. Also, KPIT's Intelligent Transport System (ITS) is India’s first ARAI certified JNNURM II compliant On-Bus ITS solution.
Growth drivers:

- Strong traction in Products and Platforms business (~4.5% of total revenues).
- Improvement in various segments of the company’s digital business – internet of things (IOT), analytics and cloud.
- Improvement in Utilization rates due to improving operational profitability.
- Participation in Government of India’s smart city mission and huge momentum in the focus areas of Smart Electric bus and ITS due to government initiatives of Smart Cities and Make in India.

The CAGR of Profit After Tax has consistently been > than 20%. The Return on Capital Employed has also been > 10% in the last 5 years.
Overall, KPIT has invested in creation of technologies for software automation, digital technologies and industry specific solutions in engineering and business IT. The results of these investments are being reflected the Q-o-Q numbers and are expected to go in coming quarters as well.

Key information

Ratios	FY 2016	FY 2015
Return on Capital Employed %	18.69	13.29
Current Ratio	2.72	1.1
Debt to Equity	0.16	0.4

MRF

MRF was founded as a toy balloon manufacturing unit in Madras (now Chennai) by an entrepreneur named MammenMappillai, it was also into making a variety of other products like gloves, squeaking toys and contraceptives. The company started tread manufacturing in 1952 and with a few years had become a major player with more than 50% market share, forcing existing MNC players to exit the business. The company had a variety of technical collaborations with B.F. Goodrich,Marangoni TRS S.p.A, Industrial Pirelli S.p.A and Uniroyal Goodrich Tyre Co. MRF has won the JD Power Asia Pacific award for highest over consumer satisfaction for 5 years in a row. The company has seen its share price rise from 500 in 2001 to over 53000/- in 2016.

Growth drivers:

- The primary advantage is that rubber prices remain weak and cheap oil has meant lower input costs and good margins.
- The company operates in the lucrative replacement market and it accounts for three quarters of its sales, this allows for higher margins compared to OEM supplies.
- R&D efforts of MRF has seen them enter higher end of the market to ensure better margins and increased capital expenditure. This will allow the company to have enough capacity on hand to meet the threat of rivals who have also expanded production capacity.

The stock remains the cheapest among its industry peers and the steady growth of car and two wheeler sales means a huge potential market for the replacement market. The company has seen a huge rise in its earnings per share over the years as shown below. It has shifted its financial year to meet Indian legal requirements.

Key information

Detail(All values in INR)	**Mar '16**	**Sep '14**	**Sep '13**
Earnings per Share(thousands)	5488.43	2117.09	1891.49
Book Value(millions)	160200.40	106519.40	85947.10

Stovec Industries Limited

Stovec is a part of SPGPrints Group, The Netherlands and is a Market leader in India for Rotary Screensand Printing Machines. Stovec essentially operates in three verticals viz. Textile Printing, Graphics Printing and Sugar Filtration.

Segment Wise sales performance of the company is as follows:

Amount in millions

Verticals	2015	2014
Textile Consumables & Textile machinery	1286.36	791.87
Graphic Products	80.13	56.62
Galvanic	186.71	92.62

The Company has its manufacturing facility in Ahmedabad, with a strength of 162 permanent employees as on December 31, 2015.

Growth Drivers

- The International Monetary Fund (IMF) in its World Economic Outlook forecast India's economic growthat about 7.5 percent during 2016.
- The Government of India had notified the amended Textile Upgradation Fund Scheme (TUFS) which will give a boost to employment generation and exports in the textile sector.
- The organized apparel segment is expected to grow at a Compound Annual Growth Rate (CAGR) of more than 13 percent over a period of 10 years. The Government of India is expected to soon announce a new National Textile Policy, which aims at creating 35 million new jobs by way of increased investments by foreign companies, which in turn may increase the business prospects for industries related to textiles. The future of Indian Textile Industry which is a key business industry for your Company looks promising.

Key Information

Ratios	Fy2015	Fy2014
Revenue Growth %	58.48	32.44
Operating Margin %	23.82	19.52
Debt to Equity	0.00	0.00
Dividend Per Share (rs)	29.00	15.50

EClerx Services Limited

EClerx is an Indian knowledge process outsourcing company based out of Mumbai, India. It supports a diverse global client base, including the world's leading Financial Services, Broadband, Cable & Telecom, ecommerce & Retail, High Tech, Industrial Manufacturing & Distribution, Software, Media & Entertainment and Travel companies. It had a total revenue of 1.7 Billion in 2016.
Company has a strong financials with an average PBT of 35% for last 5 years. Company has offered shares buy back in Oct'16 and also market is expecting a good quarterly results announcement in Nov'16.
Growth drivers:

- Global KPO market is predicted to grow at a CAGR of around 23% from 2015 to 2019 and data analytics is the major growth driver in the KPO industry. eClerx has invested on data analytics to leverage the future growth.
- In May 2012, eClerx acquired Agilyst Inc., a specialist outsourced services provider serving the Cable& Telecom industry in US and UK and in March 2015 it acquired eCLX to enter Digital Services market.

Key Information

Ratios	**FY 2016**	**FY 2015**
Revenue Growth %	39.51	12.02
Operating Margin %	40.19	37
Debt to Equity	0.00	0.00
Current Ratio	6.83	3.10