Contents of this Note :

Key Investment Arguments **<u>In Favour</u>** of PI Industries Ltd. :

- ✔ ***Highly Credible Management*** with its Board comprising of vice president **ICICI Foundation**, ex-CEO **Bayer Crop**, ex-MD **Rallis** & Pharmacia and current Chairman **CII National Council on Agriculture**

- ✔ ***High Institutional ShareHolding*** at 24.28 % with the likes of VC firm **Sequoia Capital**, FIIs **Citigroup**, **JP Morgan**, **Fidelity** & FIs **ICICI Prudential** having invested in the company in last one year very near to current market price

- ✔ Spotless Image in exhibiting ***High Corporate Governance Standards*** making the company an apt case for commanding premium valuations on the bourses

- ✔ **<u>India's 5th Largest Agrochemical Company</u>**

- ✔ Generating **<u>26 % + RoE</u> every year since last 4 years**

- ✔ **<u>25 % + YoY Revenue Growth Visibility till FY16</u>** with Expanding Margins

- ✔ Strong ***<u>Order-Book</u>* *in excess of* *<u>~INR 1650 cr.</u>*** comprising of Patented Molecules

- ✔ Exclusive or One of the Only Two ***Exclusive Supplier*** to Global Agrochemical Giants

- ✔ Exclusive ***Launch Rights of Patented Products*** for Indian Market

- ✔ Exceptional Growth Track-record wherein company has **increased its Sales at 5 Years' CAGR of 22.52 %** while **<u>PAT has increased at a 5 Years' CAGR of 77.46 %</u>**

- ✔ Consistent 20 % + YoY Growth in Revenues achieved in each fiscal over last 10 fiscals (except FY03 & FY06)

- ✔ **<u>Derisked Business Model</u>** with all Risks including Currency & Raw Material Price Fluctuations Passed on to its Clients

- ✔ Having one of **<u>India's Fastest growing Herbicide Brand</u>** 'Nominee' worth INR 100 cr. + under its portfolio

- ✔ Another ***promising patented product*** Osheen (Dinotefuran) ***launched in FY13*** which is having similar potential to reach INR 100 cr. + size within next two fiscals

- ✔ Launch Slate of Two Innovative Products every year for next Two Fiscals,

- ✔ First Phase of Jambusar Facility commercialised in January'2013 with Second Phase being planned in 2HFY14

- ✔ ***10 Years Tax Holiday for Jambusar Facility*** to aid in Expanding already high PAT Margins significantly in the Medium Term

- ✔ One of the ***most efficient companies of India next to Rallis*** in Agri-Input Segment and next to ***Divis Lab***. In CSM segment

- ✔ **<u>Trading at Historically Lowest Valuations inspite of all Parameters</u>** – Business Visibility & Financials – **<u>at their Historical Best</u>** evident from its recent Q3FY13 results wherein even in a difficult business environment, company posted a ***strong 48.61 % YoY Growth in Revenues & a 51 % YoY Growth in EBITDA***

Key Investment Arguments **<u>Against</u>** PI Industries Ltd. :

- ✗ **<u>Agro-Climatic Risks</u>** for Agri-Input Segment as Indian Agriculture Sector is very much dependent on Monsoons. However, ***PI Industries is better placed than most of its Agri-Input peers*** including Rallis because of its ***~50 % (FY13e) contribution from CSM Segment*** which is backed by firm Order-Book and is insulated from domestic agro-climatic risks

- ✗ **<u>Delivery Risks in CSM Segment</u>** as company has to meet its client's delivery schedules wherein it is an exclusive or one of the only two exclusive suppliers to its client for the respective products. PI Industries has so far demonstrated robust capabilities to serve its clients in-time because of which it has been able to forge strong long term relationships with global innovators for their patented assignments

Why PI Industries Ltd. [NSE – PIIND ; BSE – 523642] deserves to be a part of one's core portfolio :

(1) A **Unique, Differentiated Business Model** which ensures robust growth visibility **(>25 % topline & >40 % bottomline per annum)** for the company atleast till FY16 is the first and foremost investment argument working in favour of PI Industries Ltd.. Its rare to find companies with such scalable business model, especially at a scale of operation which should approach **INR 1100 cr.** in FY13. Unique aspects of such business model are :

(a) A Certain **25 % + yearly growth visibility** in Revenues supported by ***robust Order-Book (~INR 1650 cr.)*** which is 2-2.5 times company's actual reported revenues (CSM) at any given point of time. Such Order-Book is also derisked to a great extent as it is supported by the clause of **'Take-or-Pay'** which shifts onus of the success of molecules (of which the said order-book comprises) on the client and therefore ensures secured revenue stream for the company. Such good flexibility is enjoyed by the company because of its proven competencies in R&D as also its hold on dealing with complex chemistry which are crucial for the commercialisation of any innovative (patented) molecules.

(b) Sustained Growth Visibility for many years as the **Order-Book comprises of patented molecules** which are in early stage of their lifecycle and therefore enjoy atleast 10 years of rising growth post commercialisation. There are three aspects to these :

- Client only contracts for the minimum offtake it expects from the commercialisation of the said molecule as it has to obey the clause of **Take-or-Pay**. Hence, if assured quantities (covered under the order-book) are not picked up by the client, it has to compensate the company by offtaking similar quantities of other molecule.

- Since the molecule is innovative and patented, it is gradually launched in different countries post commercialisation. This ensures rising volumes of the molecule as normally, a patented molecule ***picks up maximum velocity in sales from 2nd or 3rd year post commercialisation and sales volume peaks only in its 10th year of commercialisation***.

- Since the molecule is innovative and patented, the ***client keeps only one or maximum two suppliers in early stage*** because of confidentiality involved which makes the company (PI Industries) critical in client's molecule launch roadmap. This embeds an element of surprise in delivery offtake for PI Industries as the company has to remain prepared for manufacturing substantially more than contracted quantities of the molecule if the market accepts the launch well as it is only minimum quantities that are ensured by the client via order-book while extra quantities are contracted on annual basis which are not covered under the said order-book.

(c) **Expanding EBITDA Margins with rising scale** as the company is the only one or one of the only two suppliers to its client. Hence, with the growth of client the company also grows and clients are ***agrochemical multinational-giants like Bayer, BASF, Syngenta***, etc.

(d) **Exclusive right to the company (PI Industries) for molecule's launch in India** as PI, being a key manufacturer of the molecule, is the obvious choice when its client decides to launch the innovative molecule for Indian market.

To sum-up, its a unique business model formulated by the company (PI Industries) with its efforts of last two decades and the fruits of which the company is bound to enjoy atleast for the foreseeable decade. Having detailed out the key aspects of the business model above, it is necessary to understand the basics of the business model which we will do below :

PI Industries has two operating segments :

Agri-Input : under which the company, over its existence of last 50 years, has established a pan-India distribution network with own 29 branches, 10,000+ distributors/dealers which enable it to reach to 35,000+ retail points to sell Agri-Input products like insecticides, herbicides, fungicides, plant nutrients, etc. to Indian farmers.
Company is amongst top 5 agrochemical companies of India in terms of Value inspite of it having relatively smaller basket of product portfolio comprising of just 25 products till date. This is because of its focus on launching of innovative products in Indian market in tie-up with multinational innovators under a model called in-licensing via which PI gets exclusive rights to manufacture and sell products under its own brand for Indian market.

Custom Synthesis & Manufacturing (CSM) : under CSM, the company provides contract research and contract manufacturing services to multinational clients for their innovative patented molecules. PI gets involved with its clients, most of whom are large MNC agrochemical innovators, at early stage of their product lifecycle which gives the company an exclusive or one of the only two supplier status for supply of such patented molecules once they reach commercialisation stage.
PI is the only player in this segment in India focussing on patented molecules and faces competition only from the likes of Lonza, Saltigo and DSM – all foreign players.

PI's Business Model Simplified on Next Page :

An Innovator Develops a Molecule and sees its Commercial Potential.

⇩

PI gets invloved with the innovator at this stage

and takes Innovator's research further in the form of ensuring molecule's smooth transformation to commercial scale manufacture.

⇩

PI is given Assurance in the form of Long Term Contract of minimum quantity offtake with a clause of Take-or-Pay.

All the risks including currency and raw material price fluctuation are passed on to Innovator with the only risk remaining with PI that of delivery.

⇩

Molecule gets Patented and Launched at commercial level in selected countries in initial two years.

Patent Life of the molecule is usually 15-20 years.

⇩

Post successful launch in selected countries, from third year of commercialisation, product is registered in many countries simultaneously and is launched on a larger scale.

⇩

PI benefits with success of molecule as it is the exclusive or one of the two exclusive suppliers to the innovator for the molecule.

Innovator contracts for much higher quantities of the molecule than initially signed from third year of commercialisation of molecule.

⇩

PI is in a Win-Win situation.

In the event of failure of molecule, Innovator has to compensate PI for the initially contracted amount

whereas

in the event of success of molecule, PI benefits immensely as Innovator contracts for much higher quantities than initially contracted.

⇩

When this patented molecule is launched in India
PI gets the exclusive rights to sell and market the molecule under its own brand.

Note :

Global Agrochemical (Crop Protection) Industry is very concentrated with only 6 MNCs viz., Bayer, BASF, Syngenta, Dow, Dupont & Monsanto controlling >75 % Market – the other 15 % being controlled by only 4 companies, viz., Japan's Sumitomo & Arysta and Australia's Nufarm and Israel's Makhteshim

These 10 companies & couple of other small companies only innovate and develop molecules for the global market and are therefore called '**Innovators'.**

(2) **Most <u>Efficient Management of Growth</u>** is the second and most important factor that merits a closer look at this promising company from a prudent fund allocation angle. Here, we will look at three aspects :

(a) 3, 5 & 10 Years' CAGR in Revenues, EBITDA, PAT, Fixed Assets, Debt and Equity which ***signifies exceptional growth with most conservative leveraging policy as also minimal Equity Dilution***.

(b) Last 5 Years' RoE, RoCE and Debt-to-Equity parameters which ***signifies an exceptional return generated over invested capital with least Balance Sheet burden*** that exhibits the strength of the Differentiated Business Model of the company.

(c) Last 10 Years' absolute YoY Growth in Sales relative to YoY Growth in Fixed Assets as also each year's actual EBITDA & PAT margins which ***signify extreme focus of management on profitability which augurs very well for robust Cash Generation in years to come***.

Let's start straightaway :

(a)

	3 Years' CAGR	**5 Years' CAGR**	**10 Years' CAGR**
Revenue	23.83 %	22.52 %	15.65 %
EBITDA	31.30 %	35.55 %	21.14 %
PAT	50.78 %	77.46 %	34.89 %
Net Fixed Assets	26.42 %	20.49 %	18.00 %
Debt	1.31 %	7.69 %	13.57 %
Equity Share Capital **(for Fund Raising Purpose Only – Omitted Two Bonus Issues in Calculations)**	5.77 %	3.42 %	1.69 %

Four things need to be noted from above :

(i) An almost parallel 3, 5 & 10 Years CAGR in Revenue and Net Fixed Assets signify **<u>high quality growth</u>** as it is **<u>backed by rising fixed assets</u>**. Also, it leaves ample scope for the company to improve asset utilisation going forward as almost all the expansions are taken care of in last 10 years and ***going forward focus should turn to asset utilisation***.

(ii) Despite significant rise in Fixed Assets over last 10 years, ***Debt of the company shows a descending CAGR over 3, 5 & 10 Years period*** with Debt's 3 Years CAGR standing at just 1.31 % as against 3 Years CAGR in Net Fixed Assets at 26.42 % which signifies management's conservative leveraging policy wherein it has **managed the entire growth in Assets as also Revenues over last 10 years very effectively with minimal corresponding Debt increase**.

(iii) ***EBITDA & PAT have exhibited robust CAGR*** over 3, 5 & 10 Years period which is ***much higher than corresponding CAGR in Revenues*** with 5 Years' CAGR in EBITDA standing at 35.55 % and in PAT standing at 77.46 % as against 5 Years' CAGR in Revenues at 22.52 % which signifies **exceptional focus of the management on profitability** as also ability of improving quality of revenues that are coming at higher margins every passing year.

(iv) 10 Years' CAGR in Equity Share Capital standing at just 1.69 % signifies ***minimal equity dilution for achieving the robust growth*** over last 10 years period which leaves ample scope for **managing future growth quite comfortably**.

(b)

	FY12	FY11	FY10	FY09	FY08
RoE	26.5 %	35.3 %	33.7 %	29.5 %	9.42 %
5 Years' Average RoE = **26.88 %**					
RoCE	22.9 %	24.1 %	22.5 %	17.9 %	9.55 %
5 Years' Average RoCE = **19.39 %**					
Debt-to-Equity Ratio	0.7	1.0	1.2	2.1	2.5
Improvement in Debt-to-E quity over 5 Years Period = **72 %**					

Three things need to be noted from above :

(i) Consistently high RoE above 25 % and RoCE above ~20 % indicates ***most efficient use of money towards profitable growth*** as also ability of the management to ***maintain the future growth with least possible leverage***.

(ii) A significant improvement of 72 % in Debt-to-Equity from the high of 2.5 in FY08 to just 0.7 in FY12 while generating superior RoE and RoCE indicates ***conservative leveraging policy*** of the management as also ***robust cash generating ability*** of the management by formulating differentiated business model of the company.

(iii) 5 Years' Average RoE of 26.88 % and RoCE of 19.39 % indicate the company's ability to **generate exceptional returns on invested capital which is crucial for shareholders' wealth multiplication**.

(c)

	FY12	FY11	FY10	FY09	FY08	FY07	FY06	FY05	FY04	FY03
Sales Growth (YoY)	22.10 %	32.60 %	17.27 %	24.36 %	16.93 %	22.48 %	(-4.17 %)	32.38 %	25.09 %	(-20.25 %)
Net Assets Growth (YoY)	32.12 %	36.59 %	11.95 %	13.44 %	10.81 %	25.04 %	26.65 %	20.00 %	3.05 %	5.23 %
EBITDA Margin	16.59 %	15.80 %	16.13 %	13.92 %	10.15 %	10.01 %	9.52 %	10.6 %	12.18 %	9.97 %
PAT Margin	* 9.03 %	8.92 %	7.55 %	5.00 %	1.69 %	1.41 %	1.54 %	3.68 %	2.93 %	0.27 %

• PAT Margin for FY12 computed after excluding one-time gain from sale of Polymer Business. Including such one-time gain, PAT Margin for FY12 works out to be 11.45 %

Five things need to be noted from above :

(i) We have considered here YoY growth in Consolidated Sales & EBITDA (which includes both the segments viz., Agri-Input & CSM) of PI Industries Ltd.. Although company invested since 1999 in CSM segment but its real contribution started from FY08 onwards as CSM business model requires building of long-term relationships with Global Innovators which takes years, but, once such relationships are in place, ***the company has to focus only on delivery as the orders come thick and fast on a consistent basis.***

(ii) Except FY03 & FY06, ***company has delivered a <u>consistent above ~20 % YoY growth in Sales in each of the last 10 fiscal years</u>*** which is commendable. Company suffered a degrowth in Sales only in FY03 and FY06 both of which were turbulent year for Indian Agriculture Sector because of failure of monsoons as also the modern facilities that are available today not available then.

(iii) Company invested significantly in building of Assets for CSM segment over FY05 till FY07 post which it focussed on asset utilisation. FY10 signalled complete utilisation of assets of CSM segment within next 3 years which necessitated further investments into expansion in terms of building of more assets. Over FY11 and FY12 again company build assets for CSM segment – this time on a larger area and 5 times the size of the assets build previously. **<u>From FY14 onwards again the focus should turn to asset utilisation which will deliver robust sales growth with expanding margins</u>**.

(iv) Company has ***consistently improved its EBITDA and PAT margins each year over last 10 years*** which signifies company's focus on profitability. Going forward these margins are likely to significantly improve because of :

- **<u>higher contribution from high margin CSM segment</u>** (operating at 19-20 % EBITDA margin),
- Improving Asset Utilisation,
- Improving Margins of Agri-Input segment because of **<u>focus on high margin In-licensed Products</u>**, and
- Tax benefits arising of **<u>10 Year Tax Holiday of new CSM plant</u>** that will be operational from Q4FY13 onwards (which houses ***5 times the current CSM capacities***).

(v) Company has ***managed the entire CAPEX over last 10 years with consistent and significant improvement in profit margins*** while at the same time delivering consistent above 20 % YoY growth in Sales each year over last 10 years (except FY03 & FY06).

(3) High Corporate Governance Standards, Concern Towards Minority Shareholders and Business Foresightedness are the ingredients without which the last decade's consistent growth is impossible to achieve – this is where PI Industries Ltd. scores very well.

Pi is one of the few companies in India Inc. today which has the most distinguished board consisting of :

- vice-president **ICICI Foundation**,
- ex-CEO **Bayer Crop**,
- ex-MD **Rallis** & **Pharmacia**,
- Co-Chairman of **CII National Council on Agriculture**.

It is needless to say that this company possesses almost a **<u>spotless image as far as Corporate Governance goes</u>** and is one of the most transparent organisations today in :

- updating and hosting of Concalls after every quarterly results,
- having E-Voting facility in place for minority shareholders,
- maintains high disclosures in its Annual Reports (consistently since last 10 Years),
- has nil (0 %) Promoter Shareholding pledged, etc.

It will be a treat to have a glimpse at the Board of Directors (alongwith each one's background) of PI Industries below :

Salil Singhal **[Promoter & Chairman]**	➡	**Agrochemical Industry Veteran having served as Chairman of Pesticides Association of India (now Crop Care Federation) for 20 years and currently is Co-Chairman of CII National Council of Agriculture**
Mayank Singhal **[MD & CEO]**	➡	**Engineering Management Graduate from UK, is Instrumental in Rapid Growth of the Company since last decade having joined as Director in 1998 and made MD & CEO in 2009. He is the son of Chairman, Mr. Salil Singhal.**
Dr. Venkatrao Sohoni **[Board of Director]**	➡	**Agri Industry veteran having served as MD of Rallis India from 2003 till 2007 and possessing vast experience with over 40 years' in MNCs in India and USA including over 30 years' at General Management levels of Agrochemical and Pharmaceuticals businesses. Was President & MD of Pharmacia India since 1999 and was also V.P. Organisation of Pharmaceutical Producers of India (OPPI)**
Raj Kaul **[Board of Director]**	➡	**Served as Executive Director & CEO of Bayer Crop Sciences as also headed Bayer AG's M&A division for which he concluded over 200 M&A transactions in area of agrochemicals and biotechnology. Currently, he is also on the Board of Gowan Company, Yuma in Arizona (USA).**
Mrs. Ramni Nirula **[Board of Director]**	➡	**Serves as Vice-President of ICICI Foundation. Served leadership positions as Managing Director and Strategic Business Head of Corporate Banking, Investment Banking, and Rural & Agri Banking and also Project Finance at ICICI Bank Ltd. She served as the Chief Executive Officer and Managing Director of ICICI Securities Ltd. Mrs. Nirula has been associated with the ICICI Foundation for Inclusive Growth, as an Advisor**
Narayan K. Seshadri **[Board of Director]**	➡	**Started his career with Arthur Anderson in the business consultancy area. Subsequently, he joined KPMG and became the Managing Partner of the business advisory practice of the firm in India. He is also on the Board of Halcyon Resources and Management Pvt Ltd, Development Credit Bank, DHFL Venture Capital India**

Pvt Ltd, HGB Holdings Pvt Ltd, Magma Fincrop Ltd, Kalpataru Power Transmission Ltd, WABCO TVS India Ltd, SBI Capital Markets Ltd, Radiant Life Care Pvt Ltd., Halcyon Enterprises Pvt Ltd, IRIS Business Services Ltd and TVS Investments Ltd.

It is said that alongwith the Ability comes the Capability which ultimately results in the Delivery.

Foresightedness and Business Acumen of PI's management is worth talking about here in brief to assess whether this company will be able to continue posting superior growth year after year in future also :

(a) A decade back, when all Indian Agrochemical companies were focussing on introducing high-volume-low-value generics in Indian market, PI management focussed on launching medium-volume-high-value innovative products in Indian market because of which, even till date, ***company has only 25 products under its basket as compared to 70+ products all other agrochemcial companies have***.
Inspite of such a small basket of products, PI is amongst Top 5 agrochemical companies of India.

(b) A decade back, when all Indian CRAMS players (except Divis Lab.) focussed on manufacturing generics for multinationals, PI management focussed on complex chemistry involved in patented innovative molecules which involved long gestation period in building of assets and winning trust of multinationals to share their patented molecule data with an India based company. The result of this was, after a prolonged gestation period of almost 10 years, PI is ***now sitting on a scalable opportunity which is likely to enable it to post superior growth year after year consistently over many years to come***.
PI has today become India'a only company operating in this space with focus on only patented molecules and has become one of the most sought after partner of multinationals like Syngenta, Bayer, BASF, etc. for their confidential patented assignments.

(c) When company's Panoli CSM plant was likely to run out of capacities within next 3 years, management judiciously planned next expansion in FY10 at Jambusar SEZ -- first phase of which is now operational since January'2013 -- and to **capitalise fully the Tax benefits available at this new CSM facility, management immediately started drawing roadmap for second phase** at the same location for which INR 117.33 cr. funds were raised via a recent QIP issue in January'2013.

(d) To derisk company's CSM segment dependence on Agrochemical space, management inked a ***first-of-its-kind joint Research agreement with Sony Corporation of Japan*** to develop synthetic organic chemicals for Electronics Industry. PI is likely to be the exclusive manufacturer of the invention that will come out of this R&D project.

(e) To derisk company's Agri-Input segment's overdependence on its in-licensed product Nominee Gold, company recently, in FY13, ***launched an innovative product Dinotefuran (branded OSHEEN) in Indian market*** which is more effective than other products available in the marketplace today. We will discuss regarding this product in detail in next section.

It is the result of the foresightedness and proactive attitude of the management of PI that each of the company's operating segment has delivered consistent YoY growth in last five years as depicted below. **Noteworthy is the robust growth of CSM segment which is the direct result of long term relationship with innovators fructifying into numbers** :

	FY12	FY11	FY10	FY09	FY08
Agri Input Revenue (in ₹ cr.)	503	409	299	277	259
YoY Growth	**22.98 %**	**36.78 %**	**7.94 %**	**6.94 %**	**15.11 %**
Custom Synthesis & Manufacturing (CSM) Revenue (in ₹ cr.)	374	239	196	139	74
YoY Growth	**56.48 %**	**21.93 %**	**41.01 %**	**87.83 %**	**34.54 %**

(4) A novel Launch by PI in the form of Dinotefuran (Brand – OSHEEN) in July'2012 for Indian Market is the fourth and most critical factor that needs to be given due attention on by any prudent fund manager.

Dinotefuran is a patented product (broad spectrum insecticide) of Mitsui, Japan and for launching this product in Indian Market, Mitsui has collaborated with two companies viz., PI and Indofil both of whom have launched it under their own brand name (OSHEEN by PI and TOKEN by Indofil). However, PI, ***in addition to selling the product under its own brand name for Indian Market, is also manufacturing the product and supplying to Indofil***.

Let's first assess in brief the opportunity Dinotefuran provides to PI as follows before going in deep afterwards :

- Because of its success with Nominee Gold (herbicide), **PI is catering to ~5 % of total Indian Rice acreage at present** which is growing every passing year.

- Dinotefuran's main crop is Rice, for which it has proved **most effective than all other available insecticides** in preventing BPH (Brown Plant Hooper). To provide brief background of BPH – it is a pest which resulted in widespread devastation of Rice crop in India in the year 2008 and again in 2010. The yield loss reported because of this pest was as high as 50-90 % which resulted in significant loss to Indian Rice Farmers.

- PI with its established credibility amongst Indian Rice Farmers (because of its successful product Nominee Gold), will be **easily able to cross-sell Dinotefuran** as it is till date the most effective product currently available in India.

- Even if we forget here the 95 % Rice Acreage and only ***consider 5 % Rice Acreage currently served by PI Industries*** then also Dinotefuran provides a **direct cross-selling opportunity worth ~INR 350 cr. to PI**.

{ Calculation --

Total Indian Rice Acreage	= 44.4 mn. hectares
5 % of Total Indian Rice Acreage catered by PI	= 2.22 mn. hectares
2.22 mn. hectares	= 54.85 lac acres

80 grams of Dinotefuran required to treat 1 acre of paddy crop

Price of 80 gms. of Dinotefuran (OSHEEN of PI) = INR 640

54.85 lac acres x INR 640 = ₹ 351 cr.

Easily Reachable Market Opportunity for PI because of just Cross-Selling

}

- In addition, PI is also manufacturing and supplying Dinotefuran to its only other competitor in India, viz. Indofil. Hence, **PI will be the huge beneficiary of the market opportunity Dinotefuran offers for Indian market**.

Detailed Discussion of Novel Product (Dinotefuran) Opportunity for PI Industries Discussed in next 3 pages

India

World's 2nd Largest Producer of **Rice**
with
28 % Global Rice Area

Produced
104.3 mn. tonnes of Rice
from an Area of
44.4 mn. hectares

Rice Productivity in India is just
2.3 tons/hectare

v/s
China's 6.5 , US's 7.5 & Australia's 10.1 tons/hectare

(even Indonesia, Bangladesh & Vietnam have higher Rice Productivity
at 4.3, 2.9 & 4.2 tons/hectare respectively)

Cause of Rice Crop Damage

over 800 insect species damaging Rice
in one way or other but amongst them,
about **20 species are of major importance**
and of regular occurrence.
These insect pests cause huge economic loss to rice-growing farmers

Plant-hoppers and Leaf-hoppers are one of the major pests
known to infest Rice in India,
Among them, **Brown Plant hopper (BPH)** -- *Nilaparvata lugens*;
White-backed Plant hopper (WBPH) -- *Sogatella furcifera*, &
Green Leaf hopper (GLH) -- *Nephotettix virescens*
are most damaging ones.

The **BPH caused widespread devastation of Rice Crop**
during **Kharif 2008** in North India and again
during **Kharif 2010** , it was serious in sporadic pockets.
Yield loss was as high as 50-90 %.

Dinotefuran
[Effectiveness
Against BPH
v/s Other Insecticides]

Quick down action against BPH
within **24 hours of Spraying**

v/s
all existing insecticides' action against BPH
only after **3 days of Spraying**

Provides Long Duration of Control against BPH
for **20 days after Spraying**

v/s
all existing insecticides' which prevent BPH
for only **7 days after Spraying**

Can Beat Rains if Sprayed 3 hours before it

~80 gms. of Insecticide
required to be mixed with 150 liters of Water
for treating
One Acre of Crop

Case Study -- 1

in 2 Plots at Nambur Village of Guntur Territory, Andhra Pradesh – where Brown Plant hopper (BPH) was the main pest

Dinotefuran

(Launched by PI -- brand 'OSHEEN')

Dinotefuran showed 90 % control of BPH

Buprofezin

(Till Date best BPH control molecule available in the industry)

Buprofezin showed 20 % control of BPH

Case Study -- 2

in 1 Plot at Nambur Village of Guntur Territory, Andhra Pradesh – where Green Leaf hopper (GLH) was the main pest

Dinotefuran

(Launched by PI -- brand 'OSHEEN')

Dinotefuran showed **95 %** control of GLH

Buprofezin

(Till Date best BPH control molecule available in the industry)

Buprofezin showed **25 %** control of GLH

PI Ind. Advantage for Dinotefuran

Catering to ~**5 % of Total Indian Rice Acreage**
(2.22 mn. hectares = 54.85 lac Acres)
via Nominee Gold which itslef is a 100 cr.+ Product

~80 gms. of OSHEEN (Dinotefuran) required to treat 1 Acre of Paddy Crop which provides direct

Cross-Selling Market Size of ~ 350 cr. to PI Industries for OSHEEN

(80 gms. OSHEEN required in 1 Acre Paddy Crop ;
Price of 80 gms. of OSHEEN = ~INR 640 ;
54.85 lac Acres x INR 640 = INR 351 cr.)

PI already enjoys high credibility amongst Rice-growing farmers because of success of Nominee Gold which will immensely help in percolating benefits of OSHEEN amongst farmers quickly thereby

gaining of quick marketshare for OSHEEN

(5) In addition to above discussed factors like commencing of new Jambusar CSM facility (which houses 5 times the current CSM capacity) as also launch of promising product Dinotefuran (that offers immediate 350 cr. market size), another important aspect that needs a thoughtful consideration is the company's ***Debt & Interest Expenditure Analysis of Past Decade*** which clearly suggests that ***PI is on verge of entering its next significant growth phase***.

Let's first enumerate the parameters and then discuss its interpretation :

	FY12	FY11	FY10	FY09	FY08	FY07	FY06	FY05	FY04	FY03
Debt-to-Equity	0.7	1.0	1.2	2.1	2.5	2.5	1.8	1.4	0.9	1.1
Debt/N.Assets	0.61	0.87	0.72	1.09	1.08	1.08	0.91	0.83	0.62	0.82
Debt/Sales	0.26	0.34	0.27	0.44	0.47	0.50	0.41	0.28	0.23	0.37
Debt/EBITDA	1.59	2.18	1.72	3.16	4.71	5.04	4.36	2.72	1.93	3.79
Debt/PAT	* 2.93	3.87	3.67	8.82	28.22	35.62	26.97	7.85	8.03	137.37

- Debt/PAT for FY12 computed after excluding one-time gain from sale of Polymer Business. Including such one-time gain, Debt/PAT for FY12 works out to be 2.31.

	FY12	FY11	FY10	FY09	FY08	FY07	FY06	FY05	FY04	FY03
Interest Expense as % of Sales	2.29 %	2.53 %	3.37 %	4.82 %	4.77 %	4.38 %	3.91 %	2.90 %	3.91 %	5.65 %
Interest Expense as % of EBITDA	13.80 %	16.02 %	20.93 %	34.63 %	47 %	43.83 %	41.09 %	27.35 %	32.16 %	56.68 %

- Whether one looks at any of the parameter viz., Debt/Equity, Debt/Assets, Debt/Sales, Debt/EBITDA or Debt/PAT all of them are sitting at their lowest in past decade ***inspite of the fact that the revenues of the company have increased more than five-fold in the same period*** (from INR 163 cr. in FY03 to INR 877 cr. in FY12) as also ***Assets of the company have increased five-fold*** (from INR 75 cr. in FY03 to INR 375 cr. in FY12).

- Interest Expense as % of Sales & as % of EBITDA is also at its lowest in past decade ***inspite of the fact that Debt in absolute terms has increased from INR 62 cr. in FY03 to INR 232 cr. in FY12***.

- Such relatively low Debt & Interest Expense parameters ***suggest that the company is very comfortably***

placed for funding future expansions which will **<u>result in considerable increase in scale going forward even on current higher base</u>**.

- If we factor-in INR 117.33 cr. funds raised by the company via QIP in January'2013 then these parameters will further improve to suggest that ***company is now on verge of embarking on the next phase of growth***.

- History suggests that company is very conservative in its leveraging policy as also equity dilutions and management always prefers to keep debt under manageable levels and raise equity funding only when significant growth is overdue in immediate future. Whenever the ***company has gone for fund raising via equity dilution in past, it has resulted in a sharp increase in the scale of operations of the company in years immediately coming after***.

(6) So far we have discussed regarding the business model and other related aspects of PI Industries ; but, the real test of all by far discussed aspects lies in seeing whether these have enabled PI to outperform peers and therefore emerge as a superior player in its concerned industry. We will do such assessment below ---- but, before starting, an important thing needs to be noted --- the fact that PI operates under two segments viz., Agri-Input & CSM ---- and peers for each of the operating segment is different ---

Provided below is a like-to-like peer comparison for PI Industries by taking into account separate peers for each operating segment :

Agri-Input Segment Peer Comparison - YoY Revenue Growth

	9MFY13	FY12	FY11	FY10	FY09	FY08
PI Ind. (Agri-Input segment)						
YoY Growth	12.84 %	22.98 %	36.78 %	7.94 %	6.94 %	15.11 %
(Actual Revenue)	(448 cr.)	(503 cr.)	(409 cr.)	(299 cr.)	(277 cr.)	(259 cr.)
Rallis						
YoY Growth	7.81 %	10.68 %	21.44 %	5.14 %	23.06 %	(-1.01) %
(Actual Revenue)	(1058.52 cr.)	(1181.25 cr.)	(1067.26 cr.)	(900.52 cr.)	(856.16 cr.)	(695.68 cr.)
Dhanuka						
YoY Growth	13.74 %	7.38 %	20.76 %	21.13 %	35.26 %	23.91 %
(Actual Revenue)	(454.11 cr.)	(529.3 cr.)	(493.58 cr.)	(408.72 cr.)	(337.42 cr.)	(249.46 cr.)

Insecticides						
YoY Growth	13.87 %	15.91 %	19.27 %	43.25 %	33.43 %	17.49 %
(Actual Revenue)	(497.68 cr.)	(521.75 cr.)	(450.1 cr.)	(377.36 cr.)	(263.42 cr.)	(197.42 cr.)

Custom Synthesis & Manufacturing (CSM) Segment Peer Comparison – YoY Revenue Growth

	9MFY13	FY12	FY11	FY10	FY09	FY08
PI Ind. (CSM segment)						
YoY Growth	53.52 %	56.48 %	21.93 %	41.01 %	87.83 %	34.54 %
(Actual Revenue)	(370 cr.)	(374 cr.)	(239 cr.)	(196 cr.)	(139 cr.)	(74 cr.)
Divis						
YoY Growth	30.35 %	40.90 %	40.47 %	(–) 21.94 %	15.23 %	42.62 %
(Actual Revenue)	(1477.61 cr.)	(1839.49 cr.)	(1305.44 cr.)	(929.29 cr.)	(1190.56 cr.)	(724.42 cr.)
Hikal						
YoY Growth	–(0.44) %	40.66 %	(–) 7.92 %	12.13 %	58.96 %	28.66 %
(Actual Revenue)	(470.77 cr.)	(694.2 cr.)	(493.5 cr.)	(536 cr.)	(478 cr.)	(300.7 cr.)
Dishman						
YoY Growth	20.71 %	8.78 %	14.19 %	(–) 13.83 %	32.28 %	38.80 %
(Actual Revenue)	(934.25 cr.)	(1137.03 cr.)	(1045.24 cr.)	(915.35 cr.)	(1062.35 cr.)	(803.07 cr.)

Apart from just YoY Revenue Growth comparison done above, it is worthwhile to consider here another two aspects which are crucial and can't be ignored if one wants to assess the efficiency of each peer in real sense :

Product Portfolio Basket of Agri-Input Peers

PI Ind.	25	{ Generating Revenues worth INR 503 cr. }
Rallis	53	{ Generating Revenues worth INR 1181 cr. }
Dhanuka Agri	82	{ Generating Revenues worth INR 529 cr. }
Insecticides India	76	{ Generating Revenues worth INR 521 cr. }

Year from which Company started investing in CSM	
PI Ind.	1999
Divis	1991
Hikal	1999
Dishman	1995

Seven Things need to be noted from above :

(a) In Agri-Input segment, ***PI Ind. is one of the most efficient companies next to only Rallis***, which focuses on high value products and therefore derives more revenue from lesser number of products. This is the reason why from 82 products Dhanuka Agri derives INR 529 cr. revenue as also from 76 products Insecticides India derives INR 521 cr. revenue as against PI Ind.'s only 25 products from which the company derives INR 503 cr. revenues.

(b) YoY Revenue growth of Dhanuka Agri in initial years looks inflated by the merger of its group companies.

(c) Post the launch of Nominee Gold in FY10, ***PI Ind. has outperformed almost all peers in the agri-input industry***.

(d) In CSM space, ***PI Ind. is again the most efficient and consistent player amongst all peers only next to Divis Lab***.

(e) PI Ind. growth in CSM space has been consistent, linear and stable much like Divis Lab because of ***similar focus*** of both the companies ***on forging strong long-term relationships with global innovators*** – although in different space – pharmaceuticals for Divis and agrochemicals for PI.

(f) If we look back into the history of Divis and check where it had reached 12 years post starting of building business model in CSM space – the stage where PI Ind.'s CSM segment is atpresent -- then we find that scale of PI and Divis were almost similar and, infact **PI is now growing at much faster pace than even Divis :**

- Divis started investing in CSM space in 1991 – 12 years post that, in 2004 – Divis had reached a scale of operation of INR 317.28 cr. -- much similar to PI – which started investing in CSM space in the year 1999 and has, in last fiscal (FY12) – which is 12 years post that – has reached a scale of operation of INR 374 cr.

- The interesting thing is the growth trajectory of PI post FY12 i.e. current year, where, till 9MFY13 it has already reached a CSM scale of INR 370 cr. and is, in all likelihood, poised to attain a revenue of INR 545 cr. in FY13 from CSM segment. If we compare like-to-like and go back to check the revenue of Divis in its 13th year i.e. FY05 then we find that its scale of operation during that year was only INR 364.52 cr. and, infact, Divis crossed INR 500 cr. scale only in FY07 which happens to be the 15th year from which Divis started investing in CSM space.

(g) Although Hikal started investing in CSM space from the same year, 1999, (when PI also started) but, focus of Hikal was generics, i.e. high-volume-low-value molecules which is in contrast to PI Ind.'s focus which was patented molecules. This is the reason why although Hikal's scale of operations has today reached INR 694 cr. but its growth has been volatile and its balance sheet being heavy with Debt. Dishman, although started early in the year 1995, has also faced similar volatility in growth with its growth being highly non-linear.

(7) Now, the time is perfect to focus on the most important aspect without which no prudent investment decision is complete i.e., **the Valuations**.

We will look at this aspect from three angles viz.,

(a) Peer Valuations

(b) Scarcity Premium Completely Missing

(c) Trading at Historically Lowest Valuations

(a) **Peer Valuations :**

We will start where we left off the last section – the Peer Comparison -- . Since PI Ind. is operating under two segments viz., Agri-Input & CSM, and the peers for each of the segment are different, it will be fair to consider here each of the segment's peer valuations. Also, since the company (PI) only gives revenue break-up of each of the operating segment and reports EBITDA and PAT as a consolidated entity (without giving segmentwise EBITDA since assets are shared by both the segments), it will be prudent to consider here two valuation parameters viz., EV/EBITDA and EV/PAT.

- We have considered here **Enterprise Value** (rather than pure Market Cap) as it will truly reflect the valuations of each of the companies involved, and

- we have included here a parameter **EV/PAT** without which it will be impossible to reflect the correct valuations of debt-laden companies like Hikal and Dishman as ***its afterall the net profitability which matters the most and depicts the efficiency of operations of a company***.

- For fair assessment, we have also included here ***5 Years' CAGR in EBITDA & PAT as also 5 Years' Average RoE & RoCE registered by each of the company***.

Agri-Input Segment Peer Comparison							

	5 Years' CAGR in EBITDA	5 Years' CAGR in PAT	5 Years' Avg. RoE	5 Years' Avg. RoCE	EV/EBITDA (FY13e)	EV/PAT (FY13e)
PI Ind.	35.55 %	77.46 %	26.88 %	19.39 %	10.38	18.94
Rallis	16.07 %	11.78 %	23.37 %	27.64 %	12.18	20.73
Dhanuka	29.78 %	39.44 %	31.48 %	33.12 %	7.86	11.01
Insecticides	32.77 %	30.98 %	19.91 %	21.04 %	7.93	16.17

Custom Synthesis & Manufacturing (CSM) Segment Peer Comparison

	5 Years' CAGR in EBITDA	5 Years' CAGR in PAT	5 Years' Avg. RoE	5 Years' Avg. RoCE	EV/EBITDA (FY13e)	EV/PAT (FY13e)
PI Ind.	35.55 %	77.46 %	26.88 %	19.39 %	10.38	18.94
Divis	23.96 %	23.24 %	29.21 %	39.51 %	18.12	23.62
Hikal	24.65 %	9.86 %	16.8 %	10.66 %	6.05	43.73
Dishman	11.38 %	- (9.14) %	11.91 %	10.03 %	5.24	16.68

Six things need to be noted from above :

(i) PI has registered **highest 5 Years' CAGR in EBITDA and PAT amongst all the peers**.

(ii) Only Divis, Rallis and Dhanuka score above PI in terms of 5 Years' Avg. RoE & RoCE.

(iii) PI Ind. deserves to trade at much higher valuations than Dhanuka & Insecticides and closer to valuations commanded by Rallis because :

- ✔ Dhanuka & Insecticides focus more on generics whereas ***PI focuses more on in-licensed products***. Infact, its only after seeing success of PI that both the peers have recently started concentrating more on in-licensed products.

- ✔ Dhanuka & Insecticides ***don't have high margin CSM component*** in their financials which PI possess which <u>**derisks PI to a great extent from domestic agro-climatic risks**</u>.

- ✔ Dhanuka is more dependent on inputs from its key investor PE firm Lighthouse which is guiding the management since last many years on peer data and new product launches. Any detaching of relationship with said PE firm could have severe impact on the business of Dhanuka.

- ✔ PI follows a much efficient policy in domestic agri-input market like no-return of stocks, on-demand delivery of products, non-negotiable predetermined distributor margins, etc. which enables it to <u>**manage inventory and working capital situation (in case of any adversities) quite efficiently than its peers**</u> like Dhanuka & Insecticides

- ✔ The Board Structure and Corporate Governance Standards followed by PI are much more robust than that of Dhanuka & Insecticides

(iv) PI Ind. deserves to trade at much higher valuations than Hikal & Dishman and closer to valuations commanded by Divis because :

- ✔ Hikal & Dishman have a history of volatile growth (with negative growth in many fiscals) and are relatively focussing more on generics

- ✔ Hikal has a history of one of the worst forex management wherein since last many years it is continuously reporting heavy forex losses

- ✔ Hikal & Dishman both have relatively high debt and poor net profitability metrics

- ✔ The Board Structure and Corporate Governance Standards followed by PI are much more robust than that of Dishman and are at par with Divis & Hikal

(v) Since CSM segment contribution to PI's financials is increasing (will be ~50 % in FY13), ***it will be prudent to value PI more inline with valuations of CSM players*** than pure Agri-Input players

(vi) **Despite its relative superiority on all fronts, PI quotes at a discount to Hikal in terms of EV/PAT and at par with Dishman**

(b) **Scarcity Premium Completely Missing :**

It is a proven fact in equity markets that when a promising company with good growth visibility is spotted at attractive valuations, every prudent investor wants to own it – and – if the equity capital of such company is limited with least equity dilutions as also minimal free float then such company commands premium valuations by virtue of 'scarcity premium'.

In case of PI Industries, although all the factors are present like, high quality management, exceptional past track record, good growth visibility, minimal fresh equity dilutions (for fund-raising) and low free float (only 6.66 % shareholding of Public), the scarcity premium is completely missing from the valuations. We will discuss this in detail below and deal with it from two angles :

- ➔ Equity Capital History of Last Decade
- ➔ Present Major Shareholding Structure

Let's start :

Equity Capital History of Last Decade :

Original Equity (FY02) ⇨ 3.54 cr.
(35,43,754 equity shares of FV 10 each)

1:1 Bonus in FY10

Post Bonus Equity as at FY10 ⇨ 7.08 cr.
(70,87,508 equity shares of FV 10 each)

(3.54 cr. Original Equity + 3.54 cr. Equity of Bonus Shares)

1:2 Bonus in FY11

Post Bonus Equity as at FY11 ⇨ 10.63 cr.

(1,06,31,262 equity shares of FV 10 each)

(7.08 cr. FY10 Equity + 3.54 cr. Equity of Bonus Shares)

Raised INR 50 cr. from Standard Chartered Private Equity
in tranches via CCPS which were then converted into equity shares in FY11-FY12

(Final Equity Shares issued = 18,92,927 equity shares of FV 10 each)

Post Fund-Raising Equity as at FY12 ⇒ 12.52 cr.
(1,25,24,189 equity shares of FV 10 each)

(10.63 cr. FY11 Equity + 1.89 cr. Equity issued to Standard Chtd. PE)

Split Face Value of Equity Shares
from INR 10 to INR 5 in FY12

Post Split Equity as at FY12 ⇒ 12.52 cr.
(2,50,48,378 equity shares of FV 5 each)

(No Change in Equity Capital Value as only F.V. split and so only No. of Equity Shares doubled)

Equity Shares issued under ESOP to company's employees **in FY12**

(Equity shares issued = 1,18,796 equity shares of FV 5 each)

Post ESOP Equity as at FY12 ⇒ 12.58 cr.
(2,51,67,174 equity shares of FV 5 each)

(12.54 cr. FY12 Equity + 0.06 cr. Equity issued under ESOP)

Raised INR 117.33 cr. via QIP Issue from Prominent FIIs & FIs
in January'2013

(Final Equity Shares issued = 19,24,656 equity shares of FV 5 each at a price of INR 609.60 per share)

Final Equity Capital
as at 31st January 2013 ⇒ 13.54 cr.
(2,70,91,830 equity shares of FV 5 each)

(No Shares Pending Conversion)

One of the most clean equity capital history we can ever find is what PI Ind. has. Six Important things need to be noted from above :

- In FY02's original Equity Capital of 3.54 cr., ***Promoters Shareholding was 74.77 %*** with Promoters Trusted Shareholders holding a further 18.34 % Equity Capital which resulted in non-Promoter-Reachable ***Public Shareholding of only 6.89 %*** (data taken from the failed delisting attempt by the company in FY02).

- From FY02 till FY11 there were ***two bonus issues*** by the company which, **with minimal change in original shareholding structure, raised the equity capital of the company from 3.54 cr. to 10.63 cr.**

- In FY10-end, company entered into an agreement with Standard Chartered PE for raising funds worth INR 50 cr. by virtue of which 18,92,927 shares of FV 10 were issued to the PE firm in tranches in FY11 and FY12 thereby raising the equity capital from 10.63 cr. to 12.52 cr.. This was the ***first equity dilution by the company for fund raising which resulted in core promoters' shareholding going down to 63.66 % from 74.77 % without any sale of shares by the promoters***.

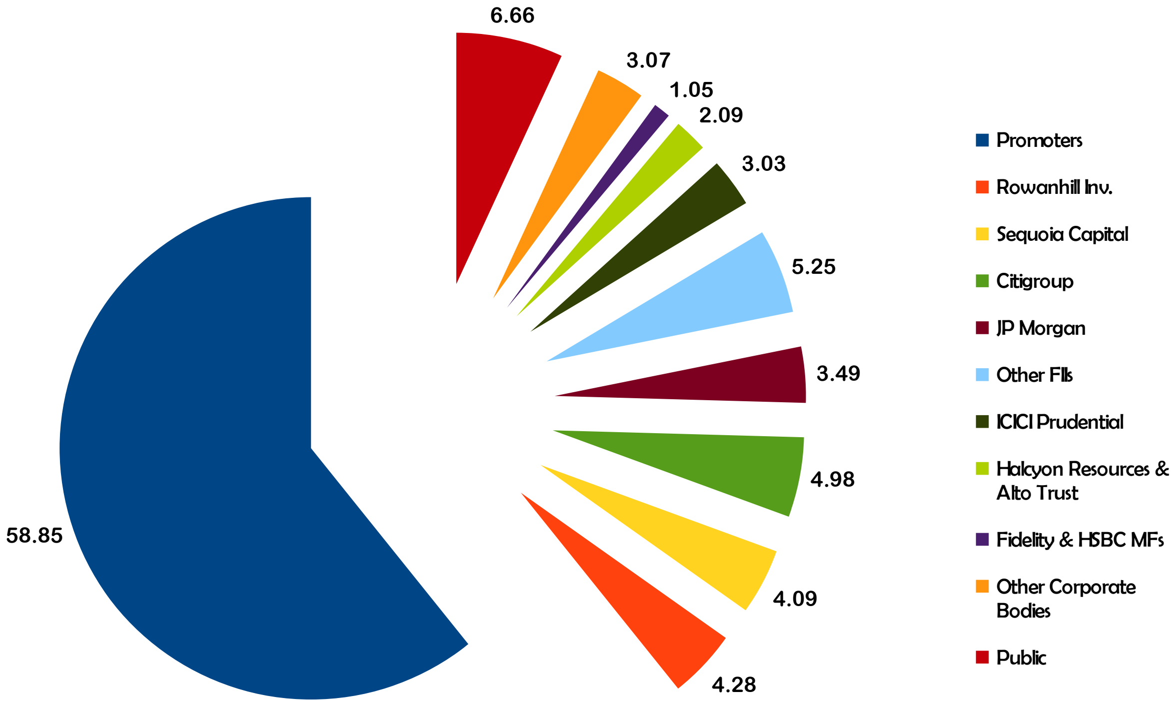
- In FY12, there was Split in face value of shares announced by the company from FV 10 to FV 5 which resulted in effective equity shares getting doubled with no corresponding change in equity capital which remained same at 12.52 cr. with same shareholding structure.

- In FY12-end, company issued 1,18,796 shares of FV 5 under ESOP to its deserving employees which resulted in its equity capital going up marginally from 12.52 cr. to 12.58 cr. with marginal drop in core promoters shareholding from 63.66 % to 63.35 %.

- Quite recently, in January'2013 (29th January 2013), company issued 19,24,656 shares of FV 5 under QIP to prominent Foreign Institutional Investors as also Domestic Institutions and raised INR 117.33 cr. which resulted in its final equity capital as on date going up to 13.54 cr. from 12.58 cr. with ***core promoters shareholding in the company going down to 58.85 % from 63.35 % without a single sale of share by the promoters***.

Now, let's first look at major shareholding structure of the company as on date before discussing further :

Present Major Shareholding Structure :



Promoters	58.85 %	
Rowanhill Investments	4.28 %	➡ Associated with the company since last two decades
Sequoia Capital (via Ironwood Investment)	4.09 %	➡ Invested Between August-December 2011 at an average buying price of **INR 528** (FV 5)
Citigroup Global	4.98 %	➡Invested in October 2012 as also picked up some shares in QIP in January 2013 at an average buying price of **INR 573** (FV 5)
JP Morgan (via Copthall Mauritius)	3.49 %	➡ Invested Between August-December 2011 at an average buying price of **INR 536** (FV 5)
Other Foreign Institutional Investors	5.25 %	➡ Invested in QIP in January 2013 at an average buying price of **INR 609** (FV 5)

ICICI Prudential Discovery Fund	3.03 %	➡ Invested in QIP in January 2013 at an average buying price of **INR 609** (FV 5)
Halcyon Resources & Alto Trust (via Narayan K. Seshadri & Govind Swarup)	2.09 %	➡ Associated with the company since 2008. Also is a board of director in PI.
Fidelity & HSBC Mutual Funds (as per their latest factsheets-holdings)	1.05 %	

- Globally renowned venture capital firm ***Sequoia Capital has invested in PI in end-2011*** at an average buying price of INR 528 (FV 5) and holds ***4.09 % stake*** in the company.

- Leading Foreign Institutional Investors led by ***Citigroup Global have invested in PI in end-2012 & beginning-2013*** at the average buying price range of INR 573-609 (FV 5) and hold ***10.23 % equity stake*** in the company.

- ***JP Morgan has invested in PI in end-2011*** at an average buying price of INR 536 (FV 5) and holds ***3.49 % stake*** in the company.

- Leading domestic fund house ***ICICI Prudential participated in the recent QIP issue*** and therefore picked up a ***3.03 % equity stake*** in PI at a price of INR 609.60 (FV 5).

- **Collectively, these and other Institutions (both foreign and domestic) hold 24.28 % equity stake in PI**. These funds, especially, VC firm Sequoia and FIIs like Citigroup and JP Morgan are long term investors and look for significant appreciation over invested capital before exit. Since ***all these funds have invested in PI in last one year with majority*** (~14.5 % equity stake holders) ***investing at a price which is not more than 4 % discount to current market price***, they are unlikely to exit from the company in medium term thereby keeping 24.28 % equity almost out of the free float.

- ***Charles Cain founded Switzerland based Private Fund CM Skye***'s investment arm Rowanhill Investment holds ***4.28 % equity stake*** in the company. It is worthwhile to note here that this fund is associated with the company since last 20 years and is infusing liquidity in company's shares in a gradual way.

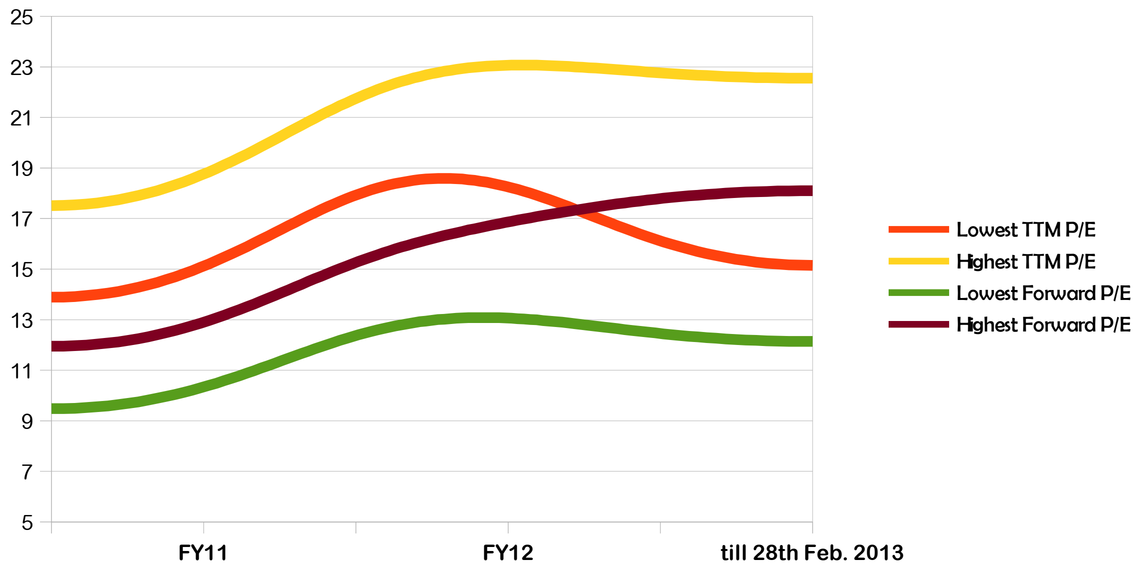
- ***Mr. Narayan K. Seshadri***, who is also a Board of Director of PI, holds ***2.09 % equity stake*** in his personal capacity as also via his associates. He is associated with the company since 2008.

➢ ***Equity Capital held by Public which is freely traded and available is just 6.66 % thereby making PI a <u>strong candidate for commanding 'scarcity premium'</u>.***

(c) **<u>Trading at Historically Lowest Valuations :</u>**

Forget the scarcity premium, -- here we have PI Ind. trading at lower range of its historically commanded multiples inspite of it having posted excellent Q3FY13 results as also its exceptional growth visibility imminent for atleast next two fiscals.

Since we are already in the last month of fiscal FY13, it is needless to say that only after passing of one month (in April'2013), the Trailing Twelve Months (TTM) commanded multiple base will shift to FY13 from current FY12 and Forward commanded multiple base will shift to FY14 from current FY13. Let's first check the historically commanded multiples of PI before moving ahead :



till FY10	**Infrequently & Intermittently Traded**
in FY10	**Thinly Traded with Average Daily Volume in FY10 at just 450 shares**

Real Trading in PI Industries Started from FY11		
	TTM P/E Multiple Range	Forward P/E Multiple Range
FY11 (trading from 1st April 2010 till 31st March 2011)	13.89 – 17.51 (Base = EPS of FY10)	9.48 – 11.95 (Base = EPS of FY11)
FY12 (trading from 1st April 2011 till 31st March 2012)	19.93 – 23.63 (Base = EPS of FY11)	13.70 – 16.66 (Base = EPS of FY12 after excluding one-time gain from sale of Polymer Business)
FY13 **(till 28th February 2013)**	15.15 – 22.55 (Base = EPS of FY12 after excluding one-time gain from sale of Polymer Business)	12.14 – 18.10 (Base = EPS of FY13e)
Average Range	16.32 – 21.23	11.77 – 15.57

If we Extrapolate Average P/E Range to FY14 and map the Actual Price Range then it comes to :

₹ 620 - 806

Seven Things need to be noted from above :

- Till FY10, PI Industries was hardly traded because of low equity capital as well as low floating stock. ***It was only after a bonus issue (1;1) in FY10 that somewhat regular trading in the company's shares started*** albeit with extremely low liquidity.

- ***Real Trading in PI Ind. shares commenced only after company raised funds from Standard Chartered PE in FY10-end*** and so the historically commanded multiples range have to be observed only from that period.

- In FY12, there was an exceptional profit because of the sale of one of the the division of the company viz., Polymer to France's Rhodia SA. Hence, for fair assessment, ***we have excluded such exceptional gain from our calculation of EPS for FY12***
(arrived at PBT excluding such exceptional gain and then arrived at PAT by deducting taxes at reasonable tax rate from said PBT).

- In our FY13e EPS calculation, ***we have factored-in dilution in equity capital on account of recent January'2013 QIP issue***. Hence, **the Forward multiples given are true reflection of commanded multiples by factoring in all the equity dilutions till date although benefits of it are likely to accrue only in FY14**.

- In our FY14 extrapolation for commanded multiple range, we have assumed a 30 % YoY growth in company's CSM segment and a modest 10 % YoY growth in domestic Agri-Input segment. In case, monsoons turn out well in 2013 and Kharif'2013 happens to be relatively better for Indian Agriculture Sector, then, FY14 projections could have substantial upsides which will in-turn push up the FY14e price range from given INR 620-806.

- We have arrived at INR 620-806 trading price range for PI Ind. for FY14 without taking into account any rerating in historically commanded multiples with :
    - rise in company's scale of operations (FY13e >1100 cr.), &
    - strong visibility of future growth on account of commencement of first phase of Jambusar project from Q4FY13 & commencement of Second Phase of the project from 2HFY14.

  Also, ***scarcity premium, which is by far completely missing from the counter, could very well catch up in case of positive triggers in the form of inorganic moves*** initiated by the management via INR 117.33 cr. funds raised from recent QIP issue.

- This is the reason why we say from one month from now on i.e from April'2013, if the current market price remains at INR 635, then, PI Ind. will be **trading at historically lowest traded multiples despite an all-round historically best improvement in varied parameters of the company**.

Conclusion :

Time is ripe to have a serious relook at this promising company as it is today sitting on verge of entering a phase which will see a significant rerating of its commanded multiples on the bourses. As you all are aware, we had initiated coverage on PI Ind. in December'2010 post which after a sharp run-up of ~84 % in company's share price, we downgraded it to a Hold on 16th February'2012 citing following concerns which cropped up then :

Concern- 1
The ***scale-up in CSM segment order book has peaked off*** since last two quarters and if such sluggish pace of addition continues for another two quarters the margin of safety reduces for the company.
Concern- 2
The revenue growth in Agri-Input segment as also the margins is so far driven mainly by Nominee Gold and just a ***slight sluggish performance of this product*** in Q2FY12 as also Q3FY12 seems to ***have a severe effect on margins*** of the segment.
Concern- 3

Company is expected to launch a blockbuster product similar to Nominee in Q1FY13 which will again ***call for significant investments*** on marketing side thereby affecting margins.

Concern- 4

Delay in commissioning of CSM plant (first it was scheduled for Q3FY12 then postponed to Q1FY13 and now again postponed to Q2FY13) doesn't augur well for the company as timely delivery is ***crucial for sensitive CSM contracts*** and any further delay could severely ***impact credibility of the company***.

It is necessary to track the **present status of each of the above concern** to check whether our conclusion about this promising company being again on verge of offering a significant wealth-creating opportunity is judicious or not. We will do such assessment below :

Concern- 1

The ***scale-up in CSM segment order book has peaked off*** since last two quarters and if such sluggish pace of addition continues for another two quarters the margin of safety reduces for the company.

Sign of its Abating :

Over the span of last six months, management has explained in length in every interaction it has had with financial community members regarding its strategy of " balancing Visibility with Flexibility ". Under this strategy, what company has done is, it has voluntarily slowed down fresh intake of large orders so as to remain flexible enough to negotiate for more lucrative deals which are in larger interest of the CSM segment of the company. The reason of this being -- they see some good patented molecule deals coming their way which could fully utilise the new Jambusar facility at exceptionally high margins. Such deals are likely to be multi-year arrangements which will improve visibility of CSM segment considerably and will establish relatively high credibility of PI in world landscape which will enable it to get recognised as a complex chemistry expert. Until these negotiations fructify, company wishes to maintain its visibility (via order-book) upto 2-2.5 years of existing + phase-1 of new Jambusar CSM facility capacities.

The new Jambusar facility has the potential to generate five times current CSM revenues of the company (~2200 cr.). The scale-up is planned in phases with each phase likely to generate ~350-400 cr. revenues within two years of operation. Hence, if management continues increasing order-book and book entirely the new Jambusar CSM facility, then, although it will increase the visibility of CSM segment but will also devoid the company of flexibility to secure lucrative deals in future which could catapult PI's CSM segment into big league......To be associated with innovators in their most complex and huge projects is what is the vision of the company and this can be done only when facility and capacity is ready to be shown to innovators.

Another important point to note with regards to order-book of CSM segment of PI, which was so far ignored by all of us is that PI's CSM order-book is actually understated. Around 40% of its CSM revenue is via annual contracts and because PI is either the sole or second supplier, a major portion of this revenue recurs every year. The balance 60% revenue is from long-term contracts executable over three to four years. The company includes only those orders executable over three-four years in its order book, which understates its total order book position.

Concern- 2

The revenue growth in Agri-Input segment as also the margins is so far driven mainly by Nominee Gold and just a ***slight sluggish performance of this product*** in Q2FY12 as also Q3FY12 seems to ***have a severe effect on margins*** of the segment.

Sign of its Abating :

Company has taken effective steps by launching two products, one miticide (Voltage) in association with Bayer and one fungicide (Clutch) in association with BASF in FY12 to mitigate the risk of over-dependency on Nominee Gold. In addition, the main reason why this concern is diminishing fast is because of company's recent product launch in the form of insecticide OSHEEN which offers both, the cross-selling opportunity to PI as well as huge potential market because of its effectiveness. It is advisable to refer to Page No. 14-18 of this Research Note wherein many aspects of OSHEEN are highlighted in detail. Still to explain here in brief :

Osheen belongs to neonicotinoid insecticides group which are proving to be most effective and therefore are projected to capture atleast 38 % marketshare (from current 26 % marketshare) of entire world insecticides sales by 2017 to become top best-selling insecticide group of the world. Neonicotinoid group itself is very concentrated one comprising of just seven molecules as of date. PI already has presence in imidacloprid (via Jumbo) - the largest selling neonicotinoid insecticide as well as the largest selling insecticide of world and thiamethoxam (via Maxima) - second largest selling neonicotinoid insecticide of world. now, with OSHEEN, it has entered sixth largest selling neonicotinoid insecticide viz., Dinotefuran. In other words, now PI will have direct presence in 3 of the 7 neonicotinoid insecticides.

Dinotefuran will be directly pitched against the most effective insecticide against BPH (brown planthooper) of India, viz., buprofezin (Rallis's Applaud). In trials conducted before the launch, dinotefuran showed 90 % control of BPH v/s 20 % control of BPH in similar buprofezin treated plots.

Now, as we all are aware, via Nominee, PI has already reached ~5 % of the total Rice acreage of India (~2.22 mn. hectares = 5.48 mn. acres). So, in effect, it offers direct 350 cr. market only because of cross-selling of OSHEEN to farmers who use Nominee (80 gms. Dinotefuran required in 1 acre of crop -- price for 80 gms. OSHEEN = ~INR 640) ; forget here the other untapped 95 % Rice market.....

Hence, in all probability, OSHEEN is set to become 100 cr. + product for PI within a couple of years inspite of the fact that Dinotefuran market in India will be shared between PI and Indofil as Indofil's pricing is much higher than PI.

Concern- 3

Company is expected to launch a blockbuster product similar to Nominee in Q1FY13 which will again ***call for significant investments*** on marketing side thereby affecting margins.

Sign of its Abating :

As was called at that time the "Blockbuster Product" is already now launched by PI in the form of OSHEEN and expenses are well taken care of by maintaining margins in 1HFY13. Since the detail of the product was not known in Feb.2012, its cross-selling opportunity in PI's key crop Rice was not known and today we have the knowledge that OSHEEN has good cross-selling opportunity for PI which can be done by minimal investments. Hence, this concern stands largely addressed.

Concern- 4

Delay in commissioning of CSM plant (first it was scheduled for Q3FY12 then postponed to Q1FY13 and now again postponed to Q2FY13) doesn't augur well for the company as timely delivery is ***crucial for sensitive CSM contracts*** and any further delay could severely ***impact credibility of the company***.

Sign of its Abating :

There can be no argument of the fact that the new CSM facility at Jambusar missed the timeline three times in last one year. However, one can take solace from the fact that the facility is finally operational with commercial production already beginning from January'2013. Such huge plants which are going to house five times the current CSM capacities sometimes take more time to build than anticipated as state-of-the-art infrastructure need to be build and efficient, technologically advanced equipments and machinery need to be installed. The heartening thing to note here is the fact that management is planning to recoup the lost time quickly by initiating roadmap for the second phase of the project from 1HFY14 itself which will ensure sustained growth for CSM business atleast for coming 3-4 years.

We are more than happy to note that management has addressed each of the concerns with their proactive moves as a result of which all of such concerns have disappeared as on date.

History suggests that, ***good companies which prove to be exceptional long-term wealth creators always take time correction rather than price correction*** and PI Ind. is the most apt example of this fact as **at no time in its trading history on the bourses, its share price has corrected more than 30 % from the closing high achieved in any particular upmove**.

Final Verdict :

To conclude, when a prudent fund manager looks at any available Investment Opportunity (IO) , he assesses such IO from varied angles and no one or two factors in isolation could make any IO a viable IO from wealth creation point of view. It is normally multiple factors that coincide to make an IO suitable for investment and PI Ind. is one such rare IO which offers :

- ✔ ***Highly Credible Board*** comprising of vice-president ICICI Foundation, ex-CEO Bayer, ex-MD Rallis, current Chairman CII National Council of Agriculture, etc.,
- ✔ ***Spotless Image in exhibiting High Corporate Governance Standards*** as well as exhibiting Utmost Transparency in interacting with Investors & Financial Community Members,
- ✔ Exceptional Past Track-Record of ***Concern Towards Minority Shareholders Wealth Multiplication***,
- ✔ Having ***Strong Relationships with Global Innovators*** – working with them on their highly confidential Patented Molecule Assignments
- ✔ **25 % + p.a. YoY Revenue Growth Visibility till FY16** with Expanding Margins because of company's Unique Differentiated Business Model,
- ✔ Rare ***Derisked Business Model*** with almost all the Risks including Currency & Raw Material Price Fluctuations being passed on to its clients,
- ✔ Strong Growth Track-Record of Last Decade, with **5 Years' Average RoE standing at 26.88 %**,

- ✔ Least Debt Burden with D/E comfortable at 0.7,
- ✔ Outperforming Peers in each of its Operating Segment,
- ✔ ***Low Free Float with just 6.66 % Shareholding with Public*** and a **High Institutional Holding of 24.28 %** which include Globally Renowned VC firm **Sequoia**, FIIs **Citigroup**, **JP Morgan** and FIs **ICICI Prudential**, etc. having invested in the company in last one year at a price which is very near to its current market price,

Today, there is dearth of quality companies that have good corporate governance standards in place while at the same time offer a significant growth visibility over a reasonable existing scale of operations (>1100 cr.). Its a rare combination which, when found in any one company, always ***commands a significant premium on the bourses*** – but – in contrast, what we actually have is **such rare combination trading at its historically lowest valuations**. On the whiff of the smallest positive trigger, this anomaly has to get corrected with the commanded multiples getting expanded to make room for the well deserved scarcity premium.

As is consistent with our Investment Thesis, 'Preservation of Capital' is the top priority with 'Considerable Scope of Capital Appreciation' the second one. **PI Industries Ltd. concurs with both the principles** ---

--- April'2013, which marks the shift of base of TTM to FY13 and Forward to FY14, confirms the first principle as safety is highest when an IO is trading at its historically lowest commanded valuations

--- while the strong growth visibility offered by commencement of Jambusar Project & Launch of Dinotefuran offer tremendous upsides in current uncertain domestic business environment which confirms our second principle.

Key Monitorables :

Agri-Input Segment Outperformance :

Since the launch of Nominee Gold in FY10, PI has consistently outperformed all of its peers. It is necessary to keep monitoring the company's outperformance on a consistent basis.

Agri-Input Segment Product Launches :

Company is planning to launch two in-licensed products every year for next couple of years. It is necessary to closely monitor company's new product launches as well as each product profile to assess their potential with respect to Indian Market.

CSM Segment Order-Book :

As is said by the company, it is sacrificing 'Visibility' for 'Flexibility' because of which CSM order-book over last one year has remained almost stagnant at around USD 300 mn.. Although, if we consider here the actual order-execution that has taken place over last one year (~USD 75 mn.), then, the order-book has increased in absolute terms, but, considering the fact that now first phase of Jambusar facility is already operational since January'2013 with second phase likely to be operational post 2HFY14, it is necessary that the **order-book at the end of any quarter, doesn't go below USD 300 mn. in FY14 with significant additions in order-book happening before the commencement of second phase**.

CSM Segment Jambusar-First Phase Utilisation :

It is necessary to keep monitoring the utilisation of Jambusar Facility's first phase which has commenced production from January'2013. The utilisation is expected to improve gradually during 1HFY14 with a good pick-up likely from 2HFY14.

CSM Segment Jambusar-Second Phase Roadmap :

Company is likely to announce roadmap for implementation of second phase at Jambusar facility by 1HFY14. It is necessary to monitor the said roadmap and check its implementation schedule which should not be later than 1HFY15.

QIP Fund Utilisation :

Company has recently, in January'2013, raised funds worth INR 117.33 cr. via a QIP issue. It is necessary to monitor the utilisation of said funds – as to – whether such funds are only used for managing working capital requirements and towards implementation of second phase at Jambusar facility or some inorganic moves, which are long overdue, are also initiated by using the flexibility attained by virtue of raising of said funds.

Inorganic Moves :

Our analysis suggests that PI Ind. has to initiate some sort of inorganic move in either Agri-Input or CSM space to emerge as a strong, consistently growing company in the long term. Organic growth is enough to let the company grow at 25 % p.a. for coming two to maximum three fiscals but, it will be in best interest of the company, to prepare foundation for inorganic growth during CY2013 as any inorganic move will take atleast one to one a half years to integrate and deliver results.

Company has so far judiciously delayed any inorganic move because of clear growth visibility provided by its organic businesses but, with rising scale of operation, it is now high time that management decides on inorganic roadmap in the best interest of the company. It will be very important to monitor whether CY2013 sees any such step being initiated by the management of PI and if yes, then the profile and benefits of such step will be key monitorable aspects.