

Pidilite Industries

BSE SENSEX
33,136

S&P CNX
10,155

CMP: INR903
TP: INR1,065 (+18%)
Buy

Stock Info

	PIDI IN
Bloomberg	PIDI IN
Equity Shares (m)	512.8
52-Week Range (INR)	972 / 682
1, 6, 12 Rel. Per (%)	4/5/17
M.Cap. (INR b)	462.9
M.Cap. (USD b)	7.0
Avg Val, INRm	439.0
Free float (%)	30.4

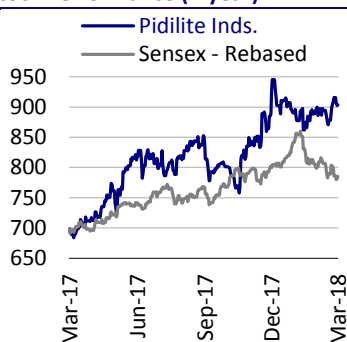
Financials Snapshot (INR b)

Y/E Mar	2018E	2019E	2020E
Net Sales	60.1	71.3	82.2
EBITDA	13.4	15.4	17.7
PAT	9.0	10.6	12.1
EPS (INR)	17.6	20.6	23.7
Gr. (%)	5.4	17.0	14.9
BV/Sh (INR)	78.2	90.0	102.0
RoE (%)	24.2	24.5	24.7
RoCE (%)	22.5	23.1	23.4
P/E (x)	51.2	43.8	38.1
EV/EBITDA (x)	33.1	28.6	24.6

Shareholding pattern (%)

As On	Dec-17	Sep-17	Dec-16
Promoter	49.0	49.0	49.0
DII	5.2	5.7	4.8
FII	36.8	36.2	37.2
Others	9.0	9.1	9.0

FII Includes depository receipts

Stock Performance (1-year)


Shift to formal trade to be faster in adhesives

We met Pidilite Industries' (PIDI) management to get an update on how its business is progressing. Key takeaways:

- In the domestic business, the existing well-penetrated categories are expected to grow at ~1.5x of GDP growth, led by repeated usage. Newer and smaller businesses, too, have the potential to grow at 2-4x of GDP growth, driven by rising penetration.
- Internationally, PIDI will now focus more on emerging markets like South-East Asia, the Middle East, Bangladesh and Thailand. Investments in the US and Brazil businesses will be put on the back burner.
- With the Goods & Services Tax (GST) now getting streamlined, management expects conversion from unorganized to organized trade to be faster in adhesives than in staples. Strict tax compliance norms are expected to test the survival of unorganized (~30% of the market) and even smaller players.
- Margins might come under pressure in the near term owing to commodity cost inflation.
- We maintain Buy on PIDI with a target price of INR1,065, based on 45x March FY20E EPS – at a 15% premium to the three-year average P/E.

Domestic business – both existing and new categories to drive sales growth

- According to management, repeated usage of its existing well-penetrated categories, along with rising penetration of the newer categories, will drive growth for PIDI. The company aims to grow at 1-1.5x of GDP growth in existing categories like adhesives, and at 2-4x of GDP growth in the other underpenetrated categories (waterproofing and construction chemicals, where penetration is less than 10%).
- Although the furniture replacement cycle has come down to 5-7 years, penetration of furniture in India – more so in smaller cities and rural areas – remains relatively low compared to global standards. However, rising disposable income of the fast-increasing middle-class population is likely to drive demand for paneling, wardrobe, and cupboards, among others. This, in turn, could boost demand for adhesives.
- Demand is back to normal 3QFY18 onward after facing the initial hiccups of demonetization and GST. Notably, PIDI has done better than consumer peers on the demand front.
- In the project and construction businesses, PIDI has taken various initiatives to educate builders and contractors regarding its product benefits, which should drive penetration and, in turn, sales.
- Demand in the waterproofing segment has been growing well. The company has roped in Mr Amitabh Bacchan as its brand ambassador for commercial campaigning. The company recommends to use the brand 'Dr Fixit' to deal with leakage at source (by mixing with cement at the time of construction) rather than waiting for the problem to emerge. PIDI is also banking on other category adjacencies to provide kicker to growth.

- PIDI invested INR964m in CIPY Polyurethanes in January 2018 to acquire a 70% stake. CIPY is engaged in the manufacture and sale of floor coatings using polyurethanes, epoxies, polyuria and polyaspartic polymers. CIPY is the market leader in floor coatings in India, catering to many industries, including food and pharma. The investment will provide PIDI with access to technology used by CIPY to participate in growth of the resin flooring and floor coatings market in India. Floor coatings are used mainly in large spaces like parking lots and factory floors, as the alternatives (e.g. tiles) are prone to chipping and accumulating dirt on the edges.
- In March 2018, PIDI entered into collaboration with Jowat SE, a German family-owned leading supplier of industrial adhesives. Through this collaboration, PIDI will now exclusively sell the entire range of Jowat adhesives in India, Sri Lanka, Bangladesh and Nepal. It will also get access to the high-growth, specialized category of hot melt adhesives, which is used in ready-made furniture.
- A JV with WD-40 (formed in Sep'16) for the sale of WD-40 brands of products in India is also doing good business.

International business – focus now on emerging markets

- On the international business (10% of sales) front, the company intends to learn from its business experience in the US and Brazil. PIDI will not be making further investments in its US and Brazil businesses. It even sold off part of the US business in June'17, while Brazil has still not turned positive at the net cash level. Against this backdrop, PIDI will now be focusing on emerging markets like South East Asia, Middle East, Bangladesh and Thailand.

GST will benefit PIDI more than consumer peers

- PIDI's key categories are now under the 18% GST bucket v/s 23-24% earlier. The company has passed on all the benefits from lower GST rates to consumers.
- GST is a short-term blip, but a far-reaching reform for the future, according to management.
- The GST system has not yet fully stabilized, according to management. Input tax credits are still claimed by one's own books of accounts (similar to VAT). Auto matching is gradually picking up – once fully functional, tax evasion is difficult. With GST now getting streamlined, management expects conversion from unorganized to organized trade to be faster in adhesives than in staples. Strict tax compliance norms are expected to test the survival of unorganized (~30% of the market) and even smaller players.
- There will also be some logistical benefits from GST with a reduction in the number of warehouses required.

Other key highlights

- Steady-state EBITDA margin expected to be ~21%.
- Witnessing signs of commodity cost inflation; VAM costs have crossed USD1,000 levels v/s USD975 at end-3QFY18.
- PIDI will take price action only if margins go beyond the band of 19-22%; this indirectly helps the company to keep competition from unorganized players at bay in an increasing raw material price scenario.

- For PIDI, a major portion of raw material is imported; large part of VAM, a key raw material, is imported from China.
- Imports (mainly raw materials) are ~USD100m on sales of ~USD 850m
- In terms of distribution, PIDI is revamping the route to market in towns with (i) population less than 50,000 and (ii) population more than 50,000 but less than 200,000 to capitalize on the rural plus small-town opportunity. A separate division called Emerging India Business has been created to explore the potential in this part of the country, where more than 80% of the population resides.
- Bangladesh operations will see commencement of the second plant in the next few months, supporting margin improvement; overall international business will also help expand margins.
- Capex for next two years to be ~USD25m/annum.

Valuation view

- PIDI offers a high-quality discretionary play with strong competitive positioning, proven in-market excellence and an impeccable track record of generating long-term shareholder value over multiple periods. Revival of volume growth and potential shift away from unorganized trade over the next 2-3 years outweigh near-term margin worries, in our view. We maintain our **Buy** rating with a target price of INR1,065 (45x Mar'19E EPS, at a 15% premium to three-year average).

Exhibit 1: WD-40 brand of products



Source: Company, MOSL

Exhibit 2: Jowat portfolio of adhesives



Source: Company, MOSL

Exhibit 3: Dr. Fixit waterproofing products – Amitabh Bacchan as brand ambassador



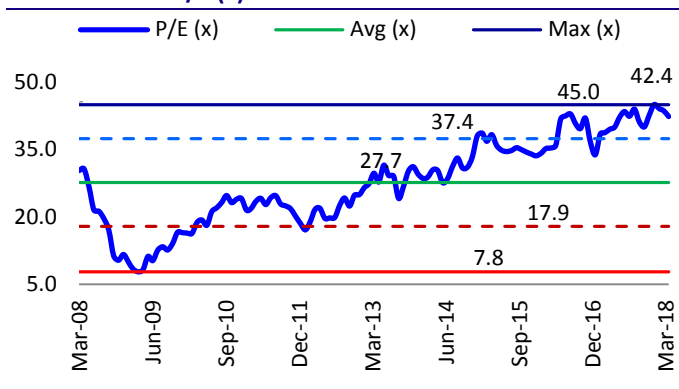
Source: Company, MOSL

Exhibit 4: CIPY – floor coating example



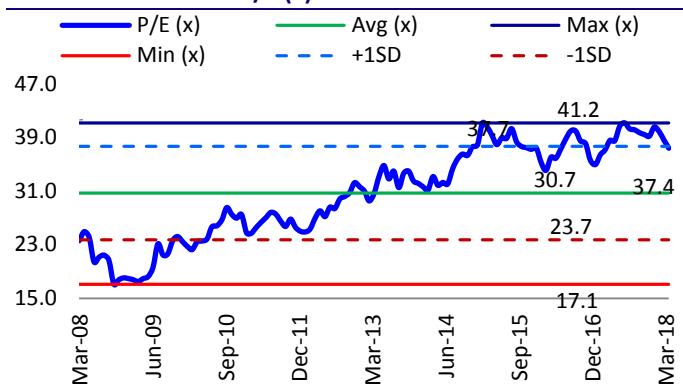
Source: Company, MOSL

Exhibit 5: PIDI P/E (x)



Source: Company, MOSL

Exhibit 6: Consumer P/E (x)



Source: Company, MOSL

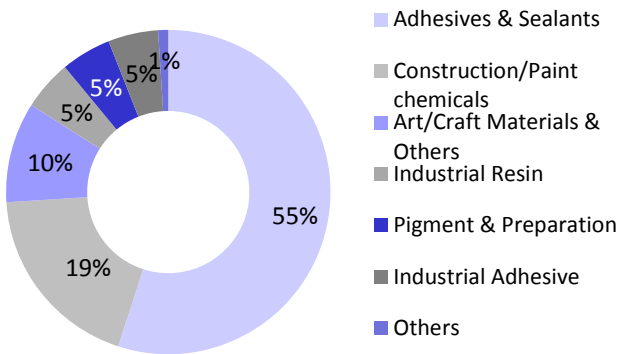
Exhibit 7: Valuation matrix

Company	Reco	CMP (INR)	Target Price		Mkt Cap		EPS Growth YoY (%)			P/E (x)			RoE (%) Div. (%)	
			(INR)	Upside (%)	(INR B)	(USD B)	FY18E	FY19E	FY20E	FY18E	FY19E	FY20E	FY18E	FY17
Consumer														
Asian Paints	Neutral	1,107	1,270	15	1,061	16.3	2.7	18.8	20.2	51.3	43.2	35.9	26.9	0.9
Britannia Inds.	Buy	4,815	5,995	24	578	8.9	14.3	24.8	25.1	57.2	45.8	36.6	33.9	0.5
Colgate-Palm.	Buy	1,040	1,365	31	283	4.3	12.9	17.9	19.7	43.4	36.8	30.7	49.9	1.0
Dabur India	Buy	319	415	30	562	8.6	4.5	19.2	16.2	42.2	35.4	30.4	25.4	0.8
Emami	Buy	1,036	1,505	45	235	3.6	-9.6	30.5	19.1	43.2	33.1	27.8	29.0	0.8
Future Cons.	Buy	56	76	37	102	1.6	Loss	LP	276.5	NM	184.3	49.0	-1.8	0.0
Godrej Cons.	Neutral	1,065	1,065	0	726	11.1	10.6	15.1	14.2	51.0	44.3	38.8	23.6	0.6
GSK C H L	Neutral	6,580	6,350	-3	277	4.2	3.1	14.1	17.4	40.9	35.8	30.5	20.7	1.1
Hind. Unilever	Buy	1,313	1,515	15	2,841	43.6	17.6	20.7	18.1	56.8	47.1	39.9	76.5	1.3
ITC	Neutral	259	278	7	3,143	48.2	6.6	13.7	12.4	28.9	25.4	22.6	22.8	2.2
Jyothy Lab.	Neutral	359	380	6	65	1.0	-27.7	32.0	24.2	44.3	33.5	27.0	13.8	1.7
Marico	Neutral	318	345	8	411	6.3	1.2	19.2	18.4	50.1	42.0	35.5	33.0	0.9
Nestle India	Neutral	7,841	7,882	1	756	11.6	13.2	13.6	20.8	56.0	49.3	40.8	43.4	0.8
P & G Hygiene	Neutral	9,121	9,303	2	296	4.5	6.9	20.5	17.3	64.2	53.3	45.4	61.2	3.5
Page Industries	Buy	20,815	27,490	32	232	3.6	24.5	39.9	32.2	70.1	50.1	37.9	39.9	0.4
Parag Milk	Neutral	261	314	20	22	0.3	147.7	38.7	35.6	29.2	21.1	15.5	10.8	0.0
Pidilite Inds.	Buy	903	1,065	18	463	7.1	5.4	17.0	14.9	51.2	43.8	38.1	24.2	0.5
United Brew.	Buy	1,002	1,380	38	265	4.1	62.0	23.9	31.2	71.2	57.5	43.8	14.9	0.1
United Spirits	Neutral	3,046	3,515	15	443	6.8	22.9	73.4	38.1	92.7	53.5	38.7	17.3	0.0
Retail														
Jubilant Food.	Neutral	2,120	2,185	3	139	2.1	186.2	29.6	31.3	69.9	53.9	41.1	22.5	0.1
PC Jeweller	Buy	361	685	90	142	2.2	44.4	26.6	27.6	23.4	18.5	14.5	16.9	0.3
Titan Company	Buy	871	990	14	773	11.9	38.8	27.0	24.1	69.5	54.7	44.1	23.4	0.4

Source: Company, MOSL

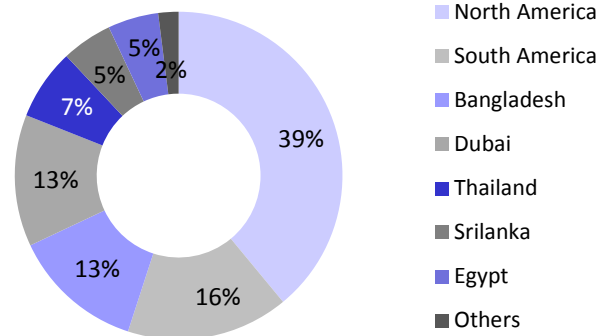
Story in charts

Exhibit 8: Segment composition (FY17)



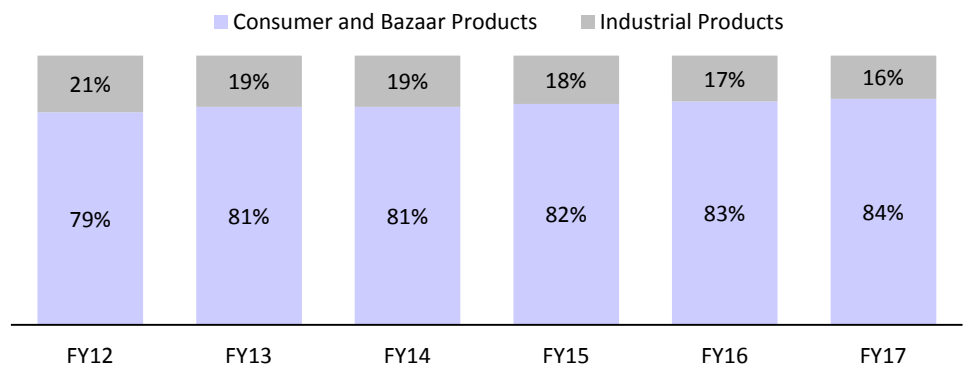
Source: Company, MOSL

Exhibit 9: International business break-up (FY17)



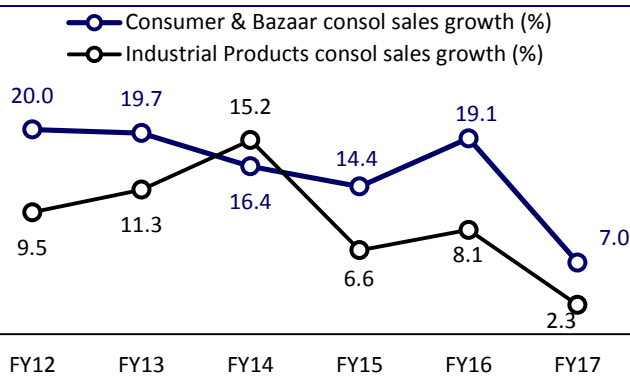
Source: Company, MOSL

Exhibit 10: Proportion of consumer and bazaar products going up over the years



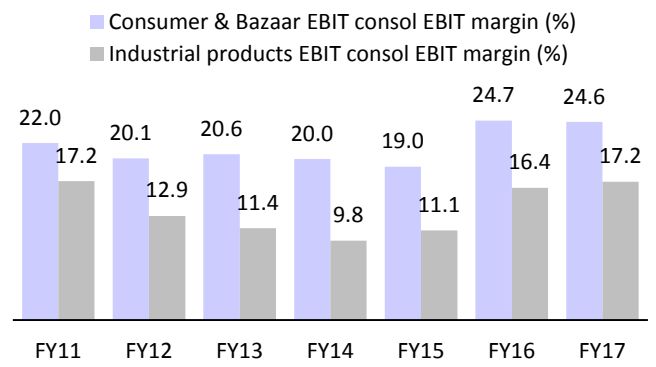
Source: Company, MOSL

Exhibit 11: Consumer and Bazaar segment grew at 15% CAGR over FY12-17...



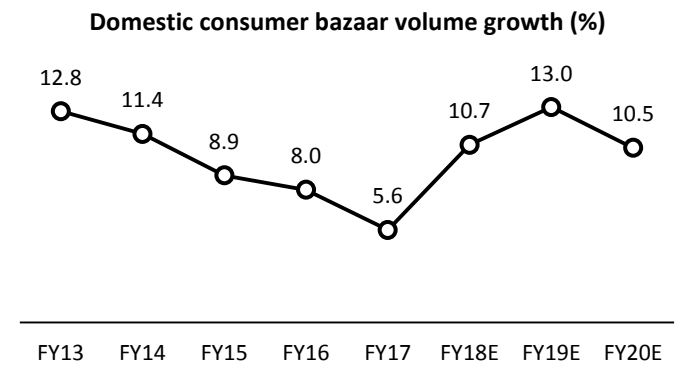
Source: Company, MOSL

Exhibit 12: ...with EBIT margins expanding 450bp YoY over the same period



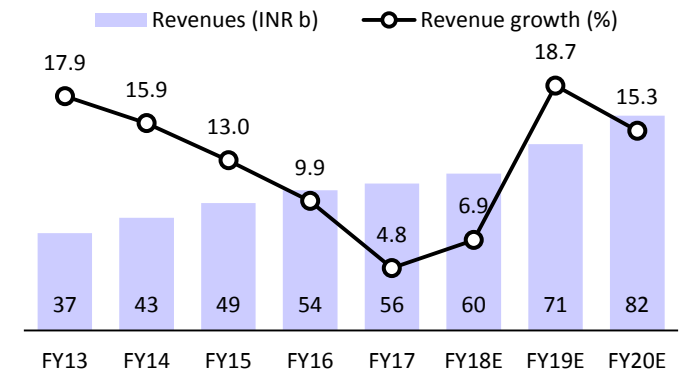
Source: Company, MOSL

Exhibit 13: Domestic consumer bazaar volumes expected to grow in double-digits going forward



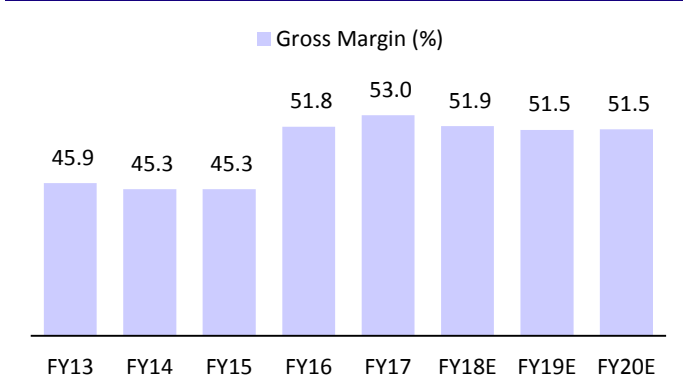
Source: Company, MOSL

Exhibit 14: Consol. sales to grow at a CAGR of 13.5% over FY17-20



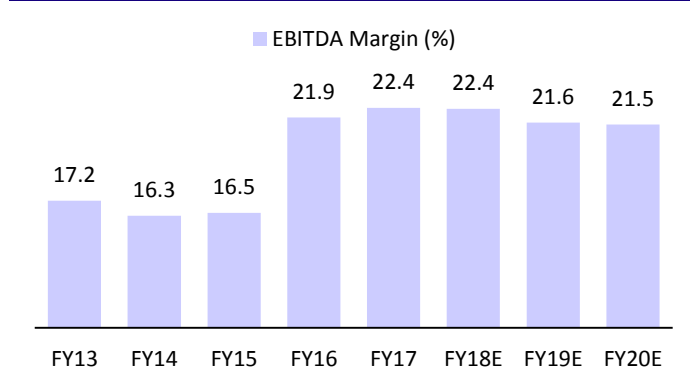
Source: Company, MOSL

Exhibit 15: Gross margins to contract 150bp over this period from unsustainable levels of FY17



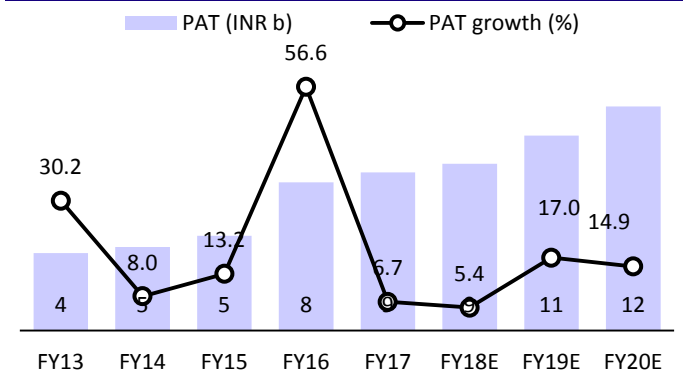
Source: Company, MOSL

Exhibit 16: ..while EBITDA margins to contract 100bp over the same period



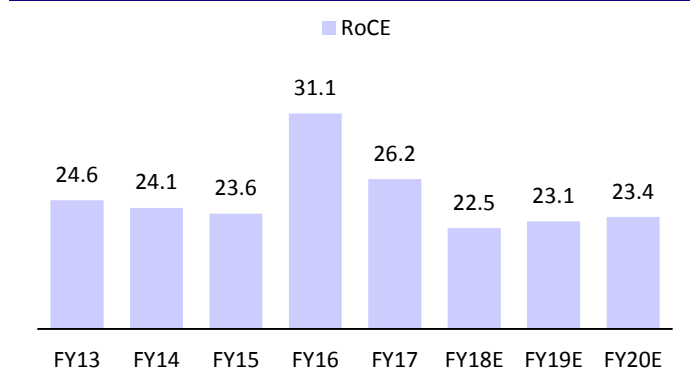
Source: Company, MOSL

Exhibit 17: Adj. PAT to grow at a CAGR of 12.3% over FY17-20



Source: Company, MOSL

Exhibit 18: RoCE (x)



Source: Company, MOSL

Financials and valuations

Income Statement							(INR Million)
Y/E March	FY15	FY16	FY17	FY18E	FY19E	FY20E	
Net Sales	48,783	53,612	56,168	60,053	71,310	82,214	
Change (%)	13.0	9.9	4.8	6.9	18.7	15.3	
Raw Materials	26,686	25,847	26,396	28,908	34,607	39,855	
Gross Profit	22,097	27,765	29,772	31,145	36,703	42,359	
Margin (%)	45.3	51.8	53.0	51.9	51.5	51.5	
Operating Expenses	14,048	16,030	17,174	17,710	21,298	24,701	
EBITDA	8,049	11,735	12,598	13,435	15,405	17,658	
Change (%)	14.2	45.8	7.4	6.6	14.7	14.6	
Margin (%)	16.5	21.9	22.4	22.4	21.6	21.5	
Depreciation	1,178	1,005	1,151	1,223	1,392	1,630	
Int. and Fin. Charges	156	133	139	159	159	159	
Other Income	113	778	1,123	1,240	1,467	1,736	
Profit before Taxes	6,828	11,376	12,430	13,292	15,321	17,605	
Change (%)	10.3	66.6	9.3	6.9	15.3	14.9	
Margin (%)	14.0	21.2	22.1	22.1	21.5	21.4	
Tax	1,694	3,335	3,851	4,254	4,750	5,458	
Tax Rate (%)	24.8	29.3	31.0	32.0	31.0	31.0	
Adj PAT	5,134	8,040	8,579	9,039	10,572	12,148	
Change (%)	13.2	56.6	6.7	5.4	17.0	14.9	
Margin (%)	10.5	15.0	15.3	15.1	14.8	14.8	

Balance Sheet							(INR Million)
Y/E March	FY15	FY16	FY17	FY18E	FY19E	FY20E	
Share Capital	513	513	513	513	513	513	
Reserves	22,193	25,867	34,196	39,571	45,644	51,793	
Net Worth	22,706	26,380	34,709	40,084	46,157	52,306	
Loans	584	800	975	1,061	1,061	1,061	
Deferred Liability	566	753	877	877	877	877	
Minority Interest	51	434	1,273	1,273	1,273	1,273	
Capital Employed	23,907	28,367	37,835	43,295	49,368	55,517	
Gross Block	17,867	17,942	20,329	22,635	24,983	27,390	
Less: Accum. Depn.	8,298	7,901	8,915	10,444	12,184	14,221	
Net Fixed Assets	9,570	10,040	11,414	12,191	12,799	13,169	
Capital WIP	4,618	1,581	1,477	1,477	1,477	1,477	
Goodwill	215	1,334	1,338	1,338	1,338	1,338	
Others	68	517	754	754	754	754	
Investments	3,599	7,055	14,431	16,431	17,931	19,431	
Curr. Assets, L&A	15,077	16,611	18,290	23,235	30,510	37,950	
Inventory	6,410	6,274	7,209	7,877	10,135	11,236	
Account Receivables	5,861	7,016	7,685	9,026	10,720	12,360	
Cash and Bank Balance	860	1,318	999	3,144	6,112	10,391	
Others	1,946	2,003	2,397	3,188	3,544	3,962	
Curr. Liab. and Prov.	9,240	8,772	9,870	12,130	15,442	18,602	
Account Payables	6,933	8,223	9,231	9,063	10,509	12,111	
Provisions	2,308	549	639	3,068	4,932	6,491	
Net Current Assets	5,837	7,839	8,420	11,104	15,069	19,348	
Application of Funds	23,907	28,367	37,835	43,295	49,368	55,517	

E: MOSL Estimates

Financials and valuations

Ratios

Y/E March	FY15	FY16	FY17	FY18E	FY19E	FY20E
Basic (INR)						
EPS	10.0	15.7	16.7	17.6	20.6	23.7
Cash EPS	12.3	17.6	19.0	20.0	23.3	26.9
BV/Share	44.3	51.5	67.7	78.2	90.0	102.0
DPS	2.9	4.2	4.2	4.5	7.5	10.0
Payout %	28.7	26.7	24.9	25.5	36.4	42.2
Valuation (x)						
P/E	90.2	57.6	54.0	51.2	43.8	38.1
Cash P/E	73.3	51.2	47.6	45.1	38.7	33.6
EV/Sales	9.4	8.5	8.0	7.4	6.2	5.3
EV/EBITDA	57.0	38.8	35.6	33.1	28.6	24.6
P/BV	20.4	17.6	13.3	11.5	10.0	8.9
Dividend Yield (%)	0.3	0.5	0.5	0.5	0.8	1.1
Return Ratios (%)						
RoE	24.3	32.8	28.1	24.2	24.5	24.7
RoCE	23.6	31.1	26.2	22.5	23.1	23.4
RoIC	39.1	45.6	40.2	38.5	42.0	46.0
Working Capital Ratios						
Debtor (Days)	44	48	50	55	55	55
Creditor (Days)	62	72	77	71	69	68
Asset Turnover (x)	3.2	3.0	2.8	2.6	2.6	2.5
Leverage Ratio						
Debt/Equity (x)	0.0	0.0	0.0	0.0	0.0	0.0

Cash Flow Statement

(INR Million)

Y/E March	FY15	FY16	FY17	FY18E	FY19E	FY20E
PBT before Extra Ord	6,828	11,376	12,430	13,292	15,321	17,605
Add: Depreciation	1,178	1,005	1,151	1,223	1,392	1,630
Interest Paid	156	133	139	159	159	159
Less: Taxes Paid	1,694	3,335	3,851	4,254	4,750	5,458
Interest income	113	778	1,123	1,240	1,467	1,736
(Incr)/Decr in WC	-718	-1,544	-900	-539	-997	0
CF from Operations	5,637	6,855	7,848	8,642	9,659	12,201
Extra ordinary items	-49	0	0	0	0	0
CFO after extraordinary	5,588	6,855	7,848	8,642	9,659	12,201
Incr in FA	-3,723	1,562	-2,422	-2,000	-2,000	-2,000
Free Cash Flow	1,864	8,417	5,426	6,642	7,659	10,201
Pur of Investments	-996	-3,456	-7,376	-2,000	-1,500	-1,500
CF from Invest.	-4,719	-1,894	-9,797	-4,000	-3,500	-3,500
Change in Networth	-3,707	-6,731	-2,698	-3,717	-4,552	-6,052
Incr in Debt	125	216	175	86	0	0
Dividend Paid	1,789	2,519	2,519	0	0	0
Interest Paid	-156	-133	-139	-159	-159	-159
Others	169	-375	1,775	1,293	1,520	1,789
CF from Fin. Activity	-1,780	-4,503	1,632	-2,497	-3,191	-4,422
Incr/Decr of Cash	-911	458	-318	2,145	2,968	4,279
Add: Opening Balance	1,772	860	1,318	999	3,144	6,112
Closing Balance	860	1,318	1,000	3,144	6,112	10,391

E: MOSL Estimates

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

In case the recommendation given by the Research Analyst becomes inconsistent with the investment rating legend, the Research Analyst shall within 28 days of the inconsistency, take appropriate measures to make the recommendation consistent with the investment rating legend.

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