

Piramal Glass

Climbing Up the "Glass Value Chain" ...

Piramal Glass- The Ajay Piramal group company with its operations spread across India, Sri Lanka & USA has presence in the Pharma, Specialty Food & Beverage (SF&B) and Cosmetics & Perfumery (C&P) segment. After acquiring the US based company "The Glass Group" (under chapter XI) in 2005, PGL made a foray in the lucrative Cosmetics & Perfumeries segment. PGL successfully turned it around and positioned itself into the premium glass segment, commanding ~6% of the global market share in C&P segment.

Investment Argument

- **Repositioning the product bouquet:** PGL is focusing on the lucrative cosmetics and perfumery segment post US acquisition. The share of C&P has increased from 30% in FY05 to 49% in FY11. With continued focus on the C&P segment and an addition of a green field 160 tpd @ Jambusar, Guj., (completely dedicated to C&P (mass)) by end FY12, PGL will endeavour to further enhance the share of C&P in its revenues. We estimate the share of C&P to rise to ~57% in FY12 and 62% in FY13.
- **Focus on the premium segment to add value:** Shifting focus from low end Pharma segment to high margin cosmetics and perfumeries along with enhanced productivity will help PGL post robust bottomline in near future. We estimate the Premium C&P segment revenue to grow at the CAGR of 28% over FY11-FY13E period. Leveraging its cost competitiveness, we estimate PGL to enhance its share in the global flocannage glass market.
- **Capex in line with Strategic intent:** PGL has lined up a capex of Rs 260 cr over the period of FY11-FY13 which includes a green field capacity of 160 tpd @ Jambusar, Guj. at an expense of Rs 100 cr and relining of the 4 furnaces in its Indian operations between FY11-FY13 at an outlay of Rs 160 cr. Post relining, the incremental capacity of the furnaces would be used for the C&P (Premium) segment. This is in line with the long term goal of the company to become one among the top 3 niche specialty (flocannage) glass manufacturers in the world.
- **Lighter balance sheet to enhance value:** PGL currently has a debt burden of Rs 920 cr (as per FY11 Consol. balance sheet) and debt/equity of 3:1. Post renegotiation, the company has been able to restructure its debt to relatively lower interest rate of 7.5% from peak rate of 13%. Going forward, we estimate the company to de-lever its balance sheet to D/E of 1.9:1 by FY13 and 1.3:1 by FY14, despite the capex programme undertaken on account of strong cash flows.

Valuation

PGL has been exhibiting a strategic shift in the product composition-moving from the commoditized, low margin SF&B/Pharma to stable, high margin C&P. We expect the company's topline to grow at a CAGR of 10% over the FY11-FY13E, and net profit to grow at 19% over the same period. We initiate BUY on the company with a price target of Rs 163 (10x FY13 EPS) which gives an upside of 50% over CMP.

Financial summary (Consolidated)

Y/E	Sales	PAT	EPS	Change	P/E	RoE	Post Tax-RoCE	EV/EBITDA	DPS
March	(Rs Cr)	(Rs Cr)	(Rs.)	(YoY %)	(x)	(%)	(%)	(x)	(Rs)
2010	1111	4	0.6	-	-	3.4	3.2	-	1.0
2011	1226	93	11.6	1989.7	-	34.2	15.0	-	3.5
2012E	1255	96	11.9	3.3	9.1	28.7	12.4	6.0	4.0
2013E	1477	131	16.3	36.8	6.7	31.9	14.1	4.8	4.0

Source: Company and ENAM estimates

BUY

CMP (Rs)	109
Target price (Rs)	163
Potential upside	50%

Stock data

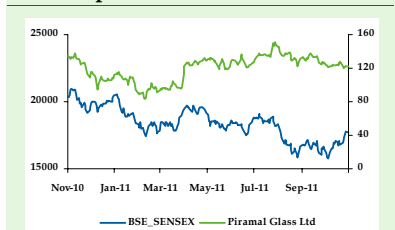
No. of shares (Cr)	8.04
FV (Rs)	10/-
Market cap (Rs Cr)	988
52 wk high/low (Rs)	156/79
Avg. daily vol* (shrs)	62002
BSE Code	532949
NSE Code	PIRGLASS
Bloomberg code	PIRA IN
Reuters Code	PRML.BO

*BSE 6 monthly

Shareholding (%)

	Sep-11	QoQ chg
Promoter	72.67	(0.01)
FIIs	0.22	(2.93)
MFs/UTI	3.3	0.86
Banks/FIs	0.04	0.04
Others	23.8	2.04

Relative performance



Source: Cline, ENAM Direct Research

Pankaj Bobade

pankaj.bobade@enam.com

BUSINESS

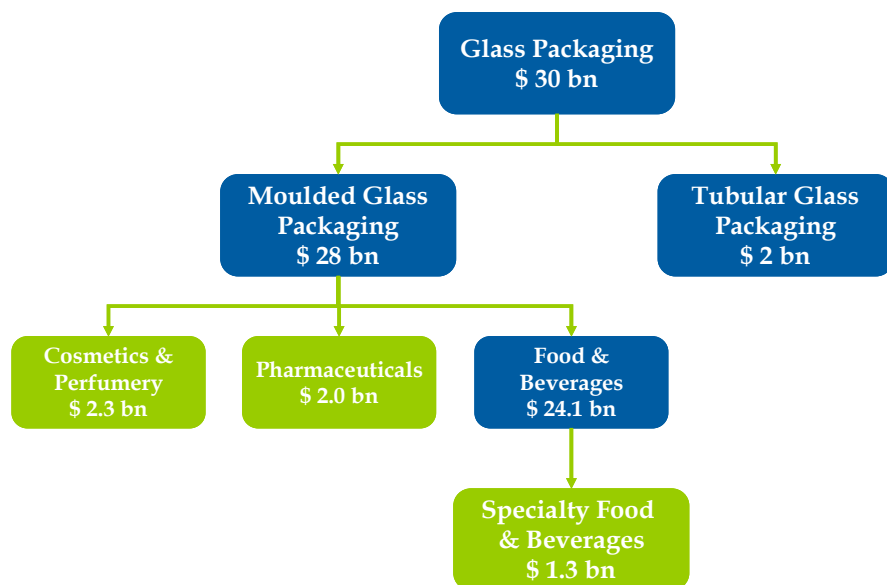
Glass maker to be reckoned with...

Piramal Glass (erstwhile Gujarat Glass) has an experience of around 25 years of glass making in India. With acquisition of Ceylon Glass, Sri Lanka in 1999 and The Glass group, US in 2005, the company made a foray in international arena. Acquisition of the US company gave PGL an access to new technology enabling an entry into the developed, niche flocannage glass market and a large customer base in the premium C&P segment (like Arden, Estee Lauder, L’Oreal, Revlon etc.). The acquisition of Glass Group has also brought with it a direct entry into the premium C&P business, an access to 17 out of the top 20 customers in the difficult to enter market marked by high gestation period of 3-5 yrs and product development cycle of 12-18 months. Post acquisition, PGL has not only turned around its US subsidiary but has commanded ~6% market share in the global flocannage glass market, making it the only Asian player to supply to the European Cosmetics and Perfume majors.

C&P segment- an opportunity to grow


Having made a foray in the C&P (mass) segment way back in FY2001 through its Indian operations by producing nail polish and low end mass perfume bottles, PGL has become a dominant player with 1 out of every 2 nail polish bottle produced globally being supplied by PGL.

Glass Packaging: Global market size



**Piramal Glass addresses niche “high value glass” market.
Addressable markets ~ 20% of overall market**

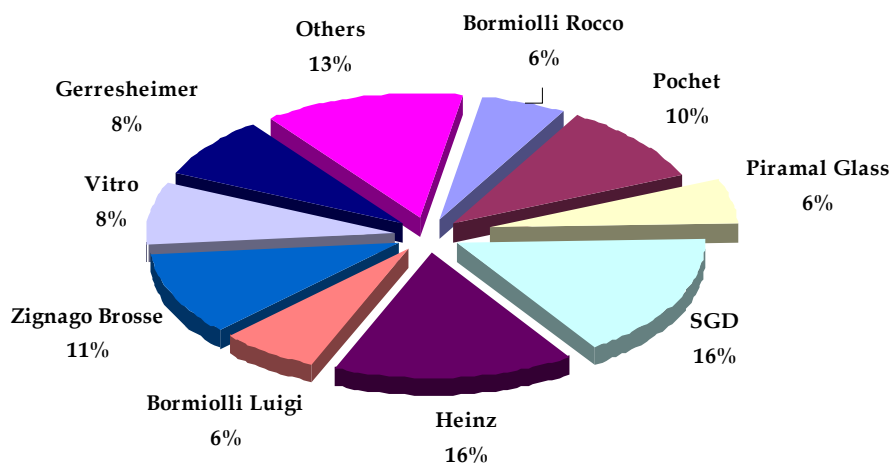
Sources: Industry reports, Market size in FY 08-09/ CY-08

 Addressable niche global markets

Source: Company, Enam Direct Research

The global glass packaging is \$30 bn in size, out of which the moulded glass packaging business is \$28 bn, which in turns can be broken up into C&P worth \$2.3 bn, Pharma worth \$2 bn and Food and beverage worth \$24.1 bn that has a subset of Specialty food & beverage of \$1.3 bn. Thus PGL addresses about 20% of the overall moulded glass market through its presence in C&P, Pharma and SF&B.

C&P market share



Source: Company, Enam Direct Research

C&P business is marked by high entry barriers viz., high quality and skill requirements, customer acquisition period of 3-5 yrs with the Cosmetics and Perfume majors, product development cycle of 12-18 months, consistent track record and concentrated customer base (20 customers constitute 80% of the market). PGL has broken into 17 large clients that include the likes of LVMH, Yves Rocher, YSL, Coty, Revlon, Unilever, Avon, Elizabeth Arden, Estee lauder etc. with US acquisition. This constitutes about 65-70% of the premium C&P market.

Typically, the high end C&P companies have tendency to develop one type of product from one source due to the complexity involved, consistency in quality required and the secrecy to be maintained till the launch of the product. The C&P majors prefer to stick with the vendors with proven and consistent track record as packaging forms an integral part of positioning the product. Sticky clients, high level human skills involved, high gestation period of 3-5 yrs, high product development cycle of 12-18 months, copy rights issues, innovation and robust product pipeline make the C&P (Premium) segment a difficult to enter market.

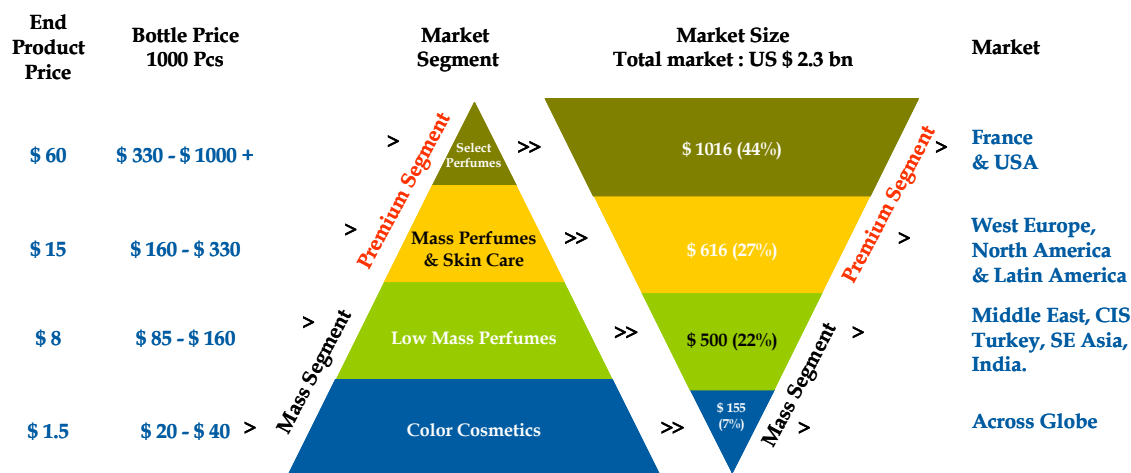
Moreover, the other large players in this segment like SGD, Gerresheimer etc are outsourcing their products to low cost destination in Asian countries. PGL being the only Asian glass maker with a proven history tends to benefit from this exercise. Chinese glass makers have failed to make any significant presence in the premium market segment mainly on account of copy right issues and communication barrier.

Growing Asian economies has led to increased consumption of skin care and perfumeries, pushing the global C&P manufacturers with established product lines to shift their bases to address this expanding market. Strong relationships of PGL with the likes of Unilever, Revlon, Avon, L’Oreal who are spreading their wings in Asian countries will come handy in garnering more share of business.

Moving up the value chain

Having made inroads, post the US acquisition, in the difficult to enter C&P business, PGL has been successfully attempting to change its product mix, gradually increasing the share of the high margin C&P business. The share of C&P segment has been growing at a faster pace than the Pharma and SF&B business resulting in topline growing at a CAGR of 24% over FY05- FY11.

Market Overview



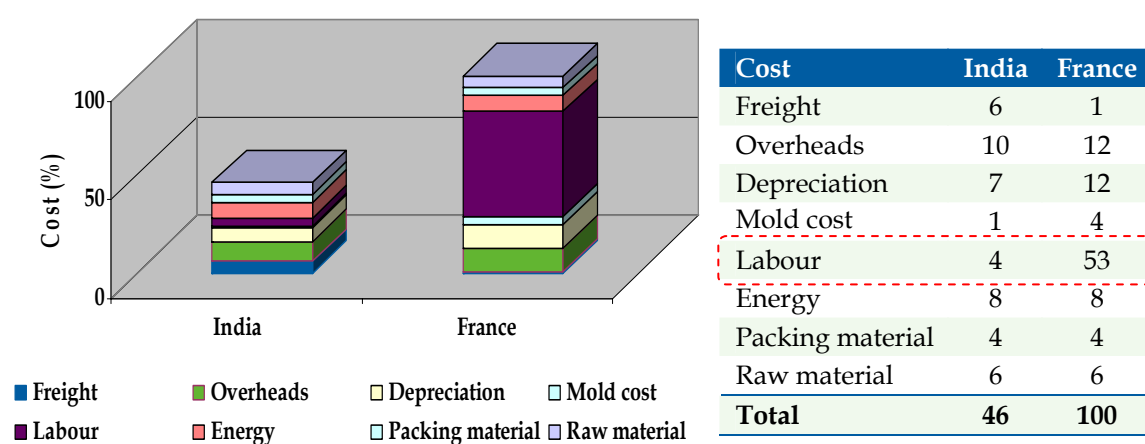
Premium constitutes about 71% of overall C&P market

Source: Company, Enam Direct Research

The cosmetic & perfumery market (worth \$2.3 bn) can be broken up into mass (29%) and premium segment (71%). Having already cornered major share in the mass segment (50% market share in color cosmetics and 10% in low mass perfumes), PGL is eyeing to hike its market share in the high margin premium segment. Currently dominated by the likes of Pochet (10.2%), SGD (16.3%), Heinz (15.7%) and Zignago Brosse (11%), the premium segment is growing at an annual CAGR of 3%. With all the advantages viz., the only Asian foccannage glass producer with established credibility, increased consumption of high end cosmetics in Asia and hence relocation of production capacity of the C&P majors in this part of world, the cost advantage on its side, we estimate PGL to post impressive growth of 28% in Premium segment and 20% in Mass segment of C&P business over the period of FY11-FY13E.

PGL enjoys a considerable cost advantage on its products vis-à-vis the European competitors. The labour costs accounts for >50% of overall product costs in Europe for C&P manufacturing as against <10% of the manufacturing cost in India thus providing a significant cost arbitrage. In addition, unlike its European peers, PGL has an in-house mould design and state of art manufacturing set up aiding it to keep a close control on the costs as well as address the issues like secrecy of the product development and infringement of copy rights. Although, PGL loses at the freight cost that it has to incur on transporting the product to the customer, the cumulative gains that the company accrues due to production at Indian operations outweighs the loss in freight.

Sustainable Cost Advantage

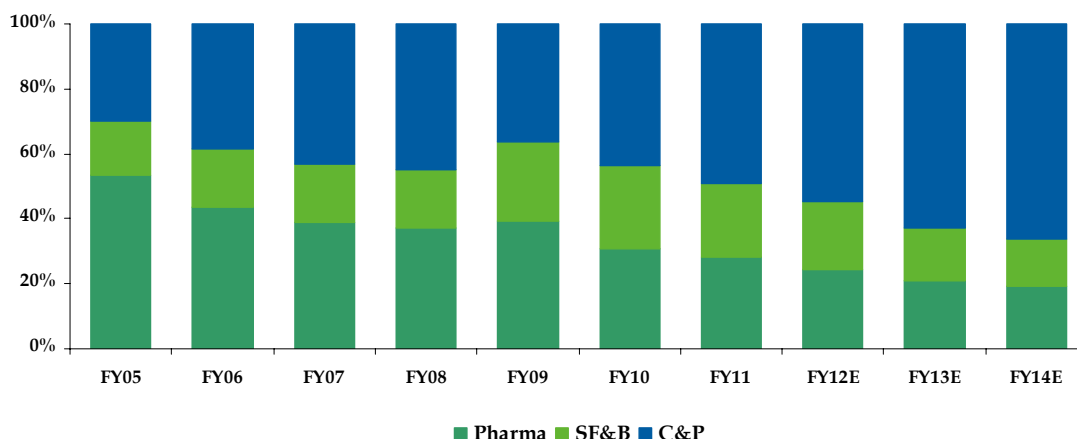


Source: Company, Enam Direct Research

Changing Product bouquet is adding value

Discreet shift in production has already started bearing fruits. PGL has been consistently exhibiting a growth rate of ~24% in topline over last 7 yrs post US acquisition. In addition, the composition of the product bouquet has also changed considerably over the same period. C&P contributed about 30% share in revenues in FY05 which has increased to about 49% in FY11. We estimate the share of overall C&P segment to exhibit a CAGR of 22% over the FY11-FY13E. Moreover, we estimate the high margin C&P-Premium segment to grow at a rate of 28% CAGR over FY11-FY13E vis-à-vis the 20% growth in the C&P-Mass over the same period.

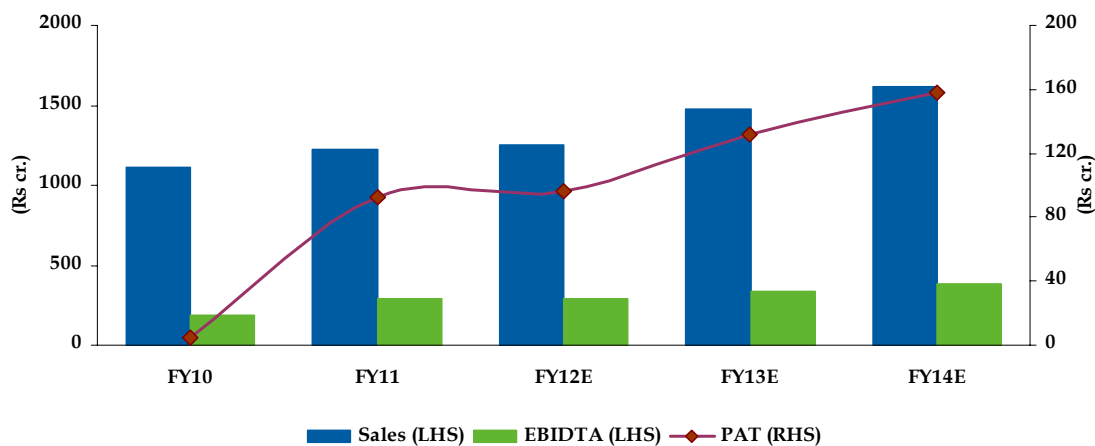
Segment wise Revenue Contribution



Source: Company, Enam Direct Research

We expect the top line growth in the FY11-FY13E period to come mainly from the C&P segment. The company has been generating free cash flow for past 2 years (refer Free Cash Flow table at the end of the report) and is expected to maintain the same going forward as the capacities are put to sweat, efficiently.

Estimated Financial Performance

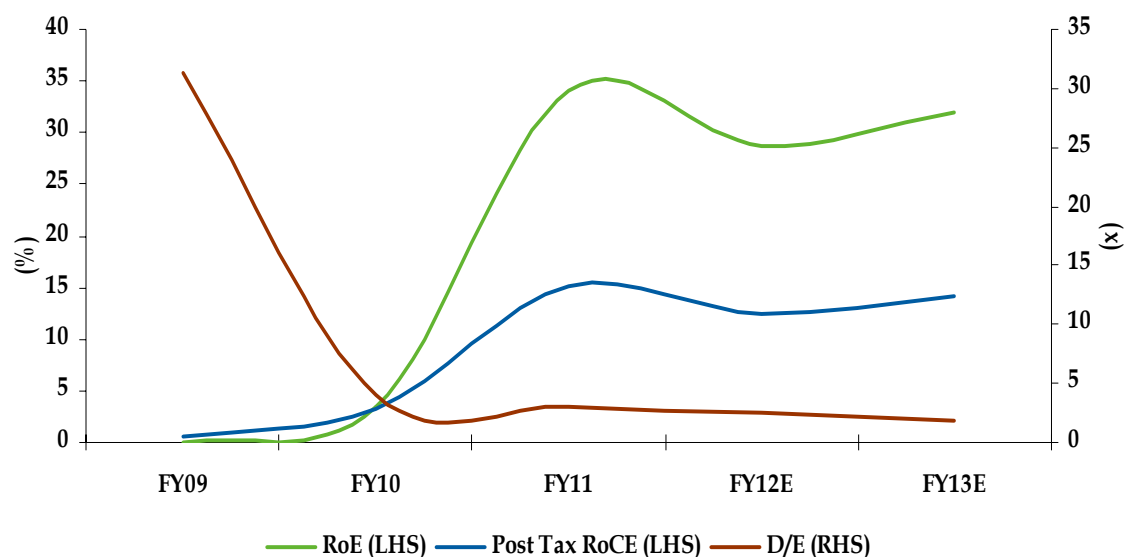


Source: Enam Direct Research

Meanwhile the debt/equity has also cascaded from the peak of 31x in FY09 to 3x in FY11. Going forward, we estimate the D/E of the company to reduce further to a reasonable 1.9x by FY13E and 1.3x by FY14E thus lightening the balance sheet despite the impending capex of Rs 260 cr.

Improving Return ratios

PGL has exhibited a sharp improvement in return ratios. The RoE in FY11 was high due to bloated leverage. In contrast, we expect the RoEs in near future to shrink slightly due to reducing leverage before perking up on account of improving profit margins (attributed to change in product mix).



Source: Direct Research

RoE break-up

(YE Mar 31st) (Rs. Cr.)	FY10	FY11	FY12E	FY13E
Net Margins (%)	0.4%	8%	8%	9%
Asset turnover (x)	0.8	1.0	1.0	1.1
RoA (%)	0.3%	7.3%	7.3%	9.6%
Leverage (x)	10.4	4.7	3.9	3.3
Return on Equity (%)	3.4%	34.2%	28.7%	31.9%

Capex cycle in its last leg

PGL has undertaken a Greenfield capacity expansion of 160 tpd dedicated to C&P- mass segment at Jambusar which is expected to be operational by end FY12 at an expense of Rs 100 cr. in addition to the relining of 4 furnaces for Rs 160 cr. The total capex of Rs 260 cr. would be funded through internal accruals. As the company is generating sufficient free cash flow, we are of the opinion that the company will not have to resort to raising fresh debt. Moreover, the company has already restructured its debt to a lower interest rate regime, which now stands at 7.5% against earlier peak rate of 13%.

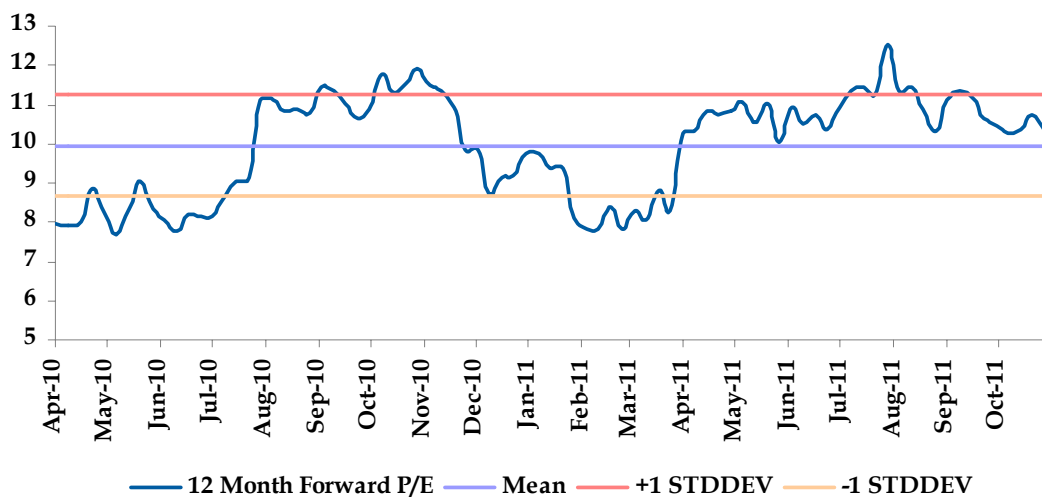
Valuations

The business model of PGL is quite robust. It has consistently been moving away from the commoditized glass packaging business to well moated business model wherein more than half of the revenues would flow in from the cosmetics & perfumery segment where it enjoys considerable cost advantage over its peers thus ensuring business even in case of a downturn in wake of the current US & European financial crisis. As the company is growing by eating away competitors' business without compromising the margins, we expect the company to post a strong growth of 10% in topline and 19% in bottomline over FY11-FY13E.

Going forward, we expect C&P business to contribute 57% and 62% of the revenues for FY12E and FY13E respectively and the Pharma and SF&B segment chipping with the rest. We expect PGL to post a topline of Rs 1477 cr and PAT of Rs 131 cr for FY13E. We have valued the company at 10x FY13E earning to arrive at a target price of Rs 163. We recommend a BUY on the company

PGL is holding a good chunk of surplus land (approx. 20 acres) in its Sri Lanka subsidiary, where it is planning to encash on the rising property prices. Any positive news on the same would be a trigger for the stock though we have not factored it in our estimates.

12 Month Forward P/E band



Source: Bloomberg

COMPANY FINANCIALS (CONSOLIDATED)

Income Statement

(Rs Cr)

Y/E Mar	FY10	FY11	FY12E	FY13E
Net sales	1,111	1,226	1,255	1,477
Cost of goods sold	791	780	834	964
Contribution (%)	29%	36%	34%	35%
Advt/Sales/Distrn O/H	134.8	158.2	134.5	174.1
Operating Profit	185	288	288	339
Other income	22	22	24	26
PBIDT	207	310	312	365
Depreciation	91	72	103	118
Interest	108	110	70	66
Other Pretax	0	(0)	0	0
Pre-tax profit	9	128	138	181
Tax provision	5	24	32	40
Minority Interests	(1)	10	10	10
Reported PAT	4	93	96	131

Balance Sheet

(Rs Cr)

Y/E Mar	FY10	FY11	FY12E	FY13E
Total assets	1,271	1,286	1,335	1,401
Gross block	1,367.3	1,517.4	1,562.1	1,619.2
Net Block	842.1	859.4	800.9	739.8
CWIP	14.1	40.2	64.2	88.2
Investments	0.1	0.1	0.1	0.1
Wkg. cap. (excl cash)	407.9	373.2	416.5	482.7
Cash / Bank balance	7.1	13.3	53.0	89.7
Capital employed	1,271	1,286	1,335	1,401
Equity capital	80.4	80.4	80.4	80.4
Reserves	159.5	221.6	281.5	376.7
Minority Interests	37.6	49.9	60.4	70.3
Borrowings	982.4	920.0	898.4	858.6
Def tax Liabilities	11.3	14.3	14.1	14.6

Source: Company, ENAM Direct Research

Ratio Analysis

(%)

Y/E Mar	FY10	FY11	FY12E	FY13E
Sales growth	9.3	10.4	2.4	17.7
OPM	16.6	23.5	22.9	23.0
Oper. profit growth	142.5	55.8	(0.2)	18.0
COGS / Net sales	71.2	63.6	66.4	65.2
Overheads/Net sales	12.1	12.9	10.7	11.8
Depreciation / G. block	6.6	4.7	6.6	7.3
Effective interest rate	9.2	11.5	7.7	7.5
Net wkg.cap / Net sales	0.4	0.3	0.3	0.3
Net sales / Gr block (x)	0.8	0.8	0.8	0.9
Post Tax RoCE	3.2	15.0	12.4	14.1
Debt / equity (x)	4.1	3.0	2.5	1.9
Effective tax rate	62.6	19.1	22.0	22.0
RoE	3.4	34.2	28.7	31.9
Payout ratio (Div/NP)	210.8	35.2	37.7	27.5
EPS (Rs.)	0.6	11.6	11.9	16.3
EPS Growth	(101.0)	1,989.7	3.3	36.8
CEPS (Rs.)	11.8	20.5	24.8	31.0
DPS (Rs.)	1.0	3.5	4.0	4.0

Cash-flow

(Rs. Cr)

Y/E Mar	FY10	FY11	FY12E	FY13E
Sources	(107)	148	152	184
Cash profit	94	175	210	260
(-) Dividends	9	33	36	36
Retained earnings	85	143	174	223
Issue of equity	62.5	0.0	0.0	0.0
Change in Reserves	133.1	3.8	0.0	0.0
Borrowings	(375)	(62)	(22)	(40)
Other	(12)	64	(0)	0.5
Applications	(107)	148	152	184
Capital expenditure	(39)	176	69	81
Investments	0	0	0	0
Net current assets	(64)	(35)	43	66
Change in cash	(5)	6	40	37

Source: Company, ENAM Direct Research

Free Cash Flow Analysis

(Rs. Cr)

	FY10	FY11	FY12E	FY13E
EBIT	94.2	215.9	184.3	221.2
Less: Adjusted Taxes	58.9	41.2	41.9	48.7
NOPLAT	35.3	174.7	142.3	172.5
Plus: Depreciation	90.7	72.0	103.3	118.2
Gross Cash flow	125.9	246.8	245.6	290.7
Less: Increase in Working Capital less cash	(49.6)	21.8	(25.8)	74.3
Operating Cash flow	175.5	225.0	271.3	216.5
Less: Net Capex	(24.1)	115.4	68.7	81.2
Less: Increase in Net Other Assets	(9.0)	(71.7)	58.8	(18.5)
FCF From Operation	208.6	181.2	143.8	153.8
Less: Inc./ (Dec.) in Investment	0.0	0.0	0.0	0.0
FCF after Investment	208.6	181.2	143.8	153.8
Plus: Gain/(loss) on Extraordinary Items	0.0	(0.0)	0.0	0.0
Total FCF	208.6	181.2	143.78	153.8

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Disclosure of interest statement (As of 2nd November, 2011)

1. Analyst ownership of the stock	No
2. Firm ownership of the stock	No
3. Directors ownership of the stock	Yes
4. MBD Relationship	No
5. Broking relationship	No

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ENAM Securities Direct Pvt. Ltd.

201, Laxmi Towers, 'A' Wing, Bandra-Kurla Complex, Bandra East, Mumbai - 400 051.

Board: 6680 3600 **Helpline:** 6680 ENAM **Fax:** 6680 3700

Website: www.enam.com / www.enamdirect.in **Email:** directresearch@enam.com