

March 8, 2010

Rating	Not Rated
Price	Rs86
Target Price	NA
Implied Upside	NA
Sensex	17,103

(Prices as on March 8, 2010)

#### Trading Data

Market Cap. (Rs bn)	6.9
Shares o/s (m)	81.0
Free Float	23.21%
3M Avg. Daily Vol ('000)	41.5
3M Avg. Daily Value (Rs m)	3.3

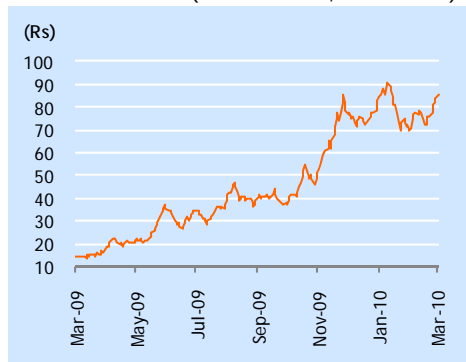
#### Major Shareholders

Promoters	76.79%
Foreign	0.01%
Domestic Inst.	0.04%
Public & Others	23.16%

#### Stock Performance

(%)	1M	6M	12M
Absolute	20.8	104.8	496.8
Relative	13.5	98.7	391.4

#### Price Performance (RIC: PRML.BO, BB: PIRA IN)



Source: Bloomberg

## Piramal Glass

### Change in product mix to improve margins

We recently met the management of Piramal Glass (PGL) to understand the business and its growth path. The key takeaways are as follows:

- **Improved relationship with major customers to increase business in C&P segment:** Out of the 20 large customers (who constitute ~80% of the market size globally), as per the management, 17 have already audited the manufacturing facility, business processes and community services. Consequently, the proportion of premium category, which fetches higher margin, is expected to increase from the current level of 46% to 63% of Cosmetics and Perfumery (C&P) sales.
- **Capex over the last 30 months to yield full benefit:** PGL invested about Rs4.5bn to expand the capacity in the C&P and pharmaceutical (pharma) segment in India by 135TPD and 70TPD, respectively and 130TPD in Specialty Food and Beverages (SF&B) segment in Sri Lanka. This has increased its capacity of glass production by 43% (in volume terms). This enhanced capacity is expected to service the premium segment.
- **US acquisition to start bearing fruits:** With established relationship with leading customers and rationalisation of manufacturing in the US and its ongoing transition to India, the US facility is expected to generate more business with improved margins.
- **Rationalize product mix in pharmaceutical and Food and Beverages (F&B) segment for profit improvement:** There has been a change in both, the market to be addressed in the F&B segment and product mix in the pharma segment. Both these segments are expected to further improve the overall margins of the company.
- **Outlook:** With US acquisition and product rationalization in all the segments, the company is expected to grow at 10-12% CAGR in sales over the next two years. At the same time, operating margin is expected to improve from current levels of 20.5% to 23% in FY11 and 25.5% in FY12.

Key financials (Y/e March)	FY06	FY07	FY08	FY09
Revenues (Rs m)	5,008	7,072	7,864	10,159
Growth (%)	49.1	41.2	11.2	29.2
EBITDA (Rs m)	718	437	1,034	762
PAT (Rs m)	171	(376)	(227)	(1,072)
EPS (Rs)	1.6	(4.8)	(2.8)	(12.5)
Growth (%)	-	-	-	-
Net DPS (Rs)	-	-	1.5	-

Source: Company Data; PL Research

Profitability & valuation	FY06	FY07	FY08	FY09
EBITDA margin (%)	14.3	6.2	13.1	7.5
RoE (%)	6.7	(21.4)	(14.2)	(102.9)
RoCE (%)	4.7	2.2	9.6	0.5
EV / sales (x)	2.4	1.8	2.0	1.9
EV / EBITDA (x)	16.4	29.5	15.2	24.9
PE (x)	52.3	(17.8)	(30.5)	(6.8)
P / BV (x)	3.5	3.8	4.3	7.0
Net dividend yield (%)	-	-	1.8	-

Source: Company Data; PL Research

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## Key Highlights

**C&P segment to be a major growth driver:** In FY09, C&P was 37% of the overall sales (currently at 42% of sales). PGL addresses both, mass as well as premium category in the C&P segment, with close to 32% of sales from premium in FY09 (currently at 46%). However, going ahead, with improved customer relationships with the top 20 customers like Coty, Procter & Gamble (P&G), Louis Vuitton (LVMH), Elizabeth Arden, L'Oreal etc. and MNC customers like Nivea, Denim, Unilever etc., the proportion of premium category which fetches higher margin is expected to increase from the current level of 46% to 63% of C&P sales. As per the management, 17 out of 20 large customers (who constitute ~80% of the market size globally) which have already audited the manufacturing facility, business processes and community services, gives PGL an edge, especially given the fact that PGL is the only player in Asia to have been approved (approval cycles can be as long as 3-4.5 years).

**Capex over the last 30 months to yield full benefit:** PGL invested about Rs4.5bn to expand the capacity in the C&P and pharma segment in India by 135TPD and 70TPD, respectively and 130TPD in Specialty Food and Beverages (SF&B) segment in Sri Lanka. This has increased its capacity of glass production by 43% (in volume terms). This enhanced capacity is expected to service the premium segment. In the initial years, the furnace catered to the low-end segment (while the premium customers were in process of approvals) and currently, has started catering to premium segments.

**US acquisition to start bearing fruits:** US forms 37% of global C&P premium segment (total global C&P premium segment is US\$1.6bn). 80% of the total US requirement is met through imports. PGL has a current market share of 10%. With established relationship with leading customers like Elizabeth Arden, Estee Lauder, L'Oreal etc. and rationalisation of manufacturing in the US and its ongoing transition to India, the US facility is expected to generate more business with improved margins. Currently, 15% of US sales are being produced in India.

**Rationalize product mix in pharma and F&B segment for profit improvement:** There has been a change in both, the market to be addressed in the F&B segment and product mix in the pharma segment. Both these segments are expected to further improve the overall margins of the company.

## Business Description

On the basis of usage of products, PGL's business can be classified as: C&P, Pharma and SF&B.

### Sales Composition

Y/e March	FY04	FY05	FY06	FY07	FY08	FY09	FY10 (YTD)
C&P	18.9	29.8	38.5	43.4	45.5	36.5	42.4
SF&B	18.9	16.7	17.8	17.7	17.6	24.1	26.8
Pharma	62.2	53.6	43.6	38.9	36.9	39.4	30.7
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>
<b>Total (Rs m)</b>	<b>3,070</b>	<b>3,360</b>	<b>4,930</b>	<b>7,010</b>	<b>7,780</b>	<b>10,090</b>	<b>8,200</b>

Source:

### Geography-wise in FY09

- BRIC forms 37% of C&P sales and Western Europe and USA forms 63% of C&P sales
- India forms 70% of pharma sales
- With respect to F&B (it being local in nature because of freight intensity), facility at Sri Lanka is used to export in Asia (specifically in India), while US facility is used to supply in the US market

### C&P Segment

This business segment can be further classified as:

- **Color Cosmetics:** PGL has 26% market share in this segment globally. It offers integrated packaging solutions through dedicated ancillary units. It enjoys leadership in launching new designs (about 40 designs a year). The company has its presence in Latin America, West Europe, Turkey and India.
- **Low mass perfumes:** PGL has a 10% market share. The C&P segment has a relatively lower margin. However, the company would cater to this segment till it gets handsome orders from other premium segments. The company designed about 60 designs per year in this segment. PGL has its presence in the Middle East, Russia, Latin America, Turkey and India.

- **MNC mass segment:** There are 20 MNC's that dominate this market as customers. PGL has recently entered (about four years ago) in this segment. The company is the only qualified vendor to MNC's in India like HUVR, L'Oreal, Revlon. The company has its presence in West Europe, North America, Latin America and India.
- **Perfume select segment:** This segment has a concentrated customer base of 20. PGL has a good relationship with 17 key customers in France and US. It has about 145 products under development in the last two years and 89 have been commercialized. PGL entered this segment through its US acquisition. With this acquisition, the company gained 10% market share in the C&P premium segment in US. The other local player has a 10% market share. The balance 80% is imported, indicating the huge potential of the market.

### SF&B Segment

PGL caters to niche market of boutique alcoholic drinks in the US. However, the company is trying to position itself as US substitute to European suppliers. In Sri Lanka, it has a market share of 88%. The company would focus on exports of specialty value-added liquor and boutique wine bottles to neighbouring markets like India, Australia and South Africa through its Sri Lankan facility.

### Pharma Segment

PGL is a market leader in India in the Pharma segment, with a market share of 35%. It also exports to over 20 countries, primarily USA. It would now focus on high value-added injectables and infusion exports. PGL would rationalize capacity in favour of high value C&P segment.

### Market size of Glass packaging industry

The Global glass packaging market size is about US\$30bn. There are two kinds of Glass packaging: Moulded Glass packaging and Tubular Glass packaging. Moulded glass packaging forms about 94%, while tubular packaging forms about 6% of the total industry size. In Moulded glass packaging, C&P forms US\$2.3bn, pharma forms US\$2bn and F&B forms US\$24.1bn. PGL is present in only Moulded glass packaging.

## USP of the business

There are large entry barriers in terms of setting up manufacturing facility and acquiring customers. As a thumb rule, Rs1.2bn-1.5bn is required to set up 100TPD furnace. It requires about 2-2.5 years to set up facility and 18-24 months to get approval from the customer to start supply. The other important entry barriers are:

- Availability of technology and skills, especially in product design, mould, cold end etc. (US acquisition and tie-up with French technicians for over a decade, gives PGL an edge)
- Presence in value-added services like decoration (providing integrated packaging solutions)
- Relationships with 17 out of 20 top customers

## Manufacturing location

It has 6 furnaces, 24 lines (Capacity-340TPD) at Kosamba (Gujarat) and 2 furnaces, 12 lines (Capacity - 335TPD) at Jambusar (Gujarat), India. It has 2 furnaces, 8 lines capacity (195TPD) at Missouri, US. It has a bottle decoration and PVC coating facility at Williamstown, New Jersey. The company also has one furnace, 5 lines, capacity (250TPD) at Horana in Srilanka

## Key Risk

PGL has total debt of Rs1.03bn and debt: equity ratio of 4:1. Even though the ratio has decreased from 14:1 in the previous year, current debt:equity ratio is not at the comfortable level.



## Outlook and Valuation

As per the management, Growth is expected to be at 10-12% CAGR in sales. However, sales composition is expected to change from lower margin products to higher margin products, specifically in the C&P segment. The company has done majority of capex of about Rs4.5bn to expand its capacity by 43% (in volume terms). At the same time, operating margin is expected to improve from 20.5% to 23% in FY11 and 25.5% in FY12. In the current year (YTD), PGL had a 600bps improvement in EBITDA margins, mainly due to improvement in product mix and turnaround of USA operations, coupled with stability in the Sri Lankan operations.

## Financials

First cut estimates						(Rs m)
Y/e March	FY09	9M FY10	FY10E	FY11E	FY12E	
Sales	10,297	8,360	11,020	12,122	13,577	
<i>Growth (%)</i>	<i>29.1</i>		<i>7.0</i>	<i>10.0</i>	<i>12.0</i>	
EBITDA	1,486	1,702	2,259	2,788	3,462	
<i>EBITDA Margin (%)</i>	<i>14.4</i>	<i>20.4</i>	<i>20.5</i>	<i>23.0</i>	<i>25.5</i>	
Interest	1,314	872	1,163	850	800	
Depreciation	893	687	900	1,050	1,100	
PBT	(721)	143	196	888	1,562	
Tax	(186)	16	-	107	281	
PAT bf ex-od item	(535)	127	196	781	1,281	
Extra ordinary item	(540)	(217)	(350)			
PAT after ex-od item	(1,075)	(90)	(154)	781	1,281	
Number of shares (m)	81	81	81	81	81	
EPS (Rs)	-		2.4	9.6	15.8	

Source: Company Data, PL Research

### Income Statement

Y/e March	FY06	FY07	FY08	FY09	9MFY10	(Rs m)
Net Sales	5,008	7,072	7,864	10,159	8,204	
<b>EXPENDITURE :</b>						
Increase/Decrease in Stock	(14)	(145)	(466)	(575)	259	
Raw Material Consumed	815	1,228	1,373	2,185	1,664	
<i>% of sales</i>	<i>16.0</i>	<i>15.3</i>	<i>11.5</i>	<i>15.8</i>	<i>23.4</i>	
Power & Fuel Cost	851	1,155	1,428	1,949	1,265	
<i>% of sales</i>	<i>17.0</i>	<i>16.3</i>	<i>18.2</i>	<i>19.2</i>	<i>15.4</i>	
Employee Cost	1,059	2,049	2,089	2,351	1,634	
<i>% of sales</i>	<i>21.1</i>	<i>29.0</i>	<i>26.6</i>	<i>23.1</i>	<i>19.9</i>	
Total other expenses	1,580	2,348	2,405	3,487	2,053	
<i>% of sales</i>	<i>31.6</i>	<i>33.2</i>	<i>30.6</i>	<i>34.3</i>	<i>25.0</i>	
Total Expenditure	4,291	6,636	6,830	9,397	6,876	
Operating Profit (Excl OI)	718	437	1,034	762	1,328	
<i>Operating profit Margin (%)</i>	<i>14.3</i>	<i>6.2</i>	<i>13.1</i>	<i>7.5</i>	<i>16.2</i>	
Other Income	235	196	223	209	157	
Operating Profit	953	633	1,256	971	1,485	
Interest	209	366	688	1,336	872	
Depreciation	519	515	693	892	687	
Profit Before Tax	226	(249)	(125)	(1,258)	(74)	
Provision for Tax	55	127	102	(186)	16	
Profit After Tax	171	(376)	(227)	(1,072)	(90)	
Minority Interest	(38)	(15)	(2)	47	(20)	
Consolidated Net Profit	133	(391)	(228)	(1,025)	(70)	

Source: Company Data, PL Research



## Balance Sheet

(Rs m)

Y/e March	FY06	FY07	FY08	FY09
<b>SOURCES OF FUNDS:</b>				
Share Capital	173	173	180	180
Total Reserves	1,830	1,479	1,379	254
<b>Shareholder's Funds</b>	<b>2,003</b>	<b>1,652</b>	<b>1,559</b>	<b>434</b>
Minority Interest	201	206	398	447
Secured Loans	3,429	4,208	4,874	5,321
Unsecured Loans	1,399	2,836	5,539	8,249
<b>Total Debts</b>	<b>4,828</b>	<b>7,044</b>	<b>10,413</b>	<b>13,571</b>
<b>Total Liabilities</b>	<b>7,032</b>	<b>8,902</b>	<b>12,369</b>	<b>14,452</b>
<b>APPLICATION OF FUNDS :</b>				
Gross Block	7,714	9,367	12,287	14,052
Less: Accumulated Depreciation	2,870	3,303	3,546	4,490
Net Block	4,844	6,064	8,741	9,562
Capital Work in Progress	143	476	301	148
Investments	0.11	0.11	0.11	0.12
<b>Current Assets, Loans &amp; Advances</b>				
Inventories	1,306	1,429	2,128	2,855
Sundry Debtors	1,177	1,406	2,018	2,688
Cash and Bank	119	61	86	118
Other Current Assets	30	57	40	37
Loans and Advances	366	1,041	1,169	732
<b>Total Current Assets</b>	<b>2,998</b>	<b>3,993</b>	<b>5,441</b>	<b>6,430</b>
<b>Less : Current Liabilities and Provisions</b>				
Current Liabilities	461	742	1,252	1,033
Provisions	261	636	581	562
<b>Total Current Liabilities</b>	<b>722</b>	<b>1,378</b>	<b>1,833</b>	<b>1,595</b>
<b>Net Current Assets</b>	<b>2,276</b>	<b>2,615</b>	<b>3,608</b>	<b>4,834</b>
Miscellaneous Expenses not written off	10	-	-	-
Deferred Tax Assets / Liabilities	(241)	(253)	(280)	(93)
<b>Total Assets</b>	<b>7,032</b>	<b>8,902</b>	<b>12,369</b>	<b>14,452</b>

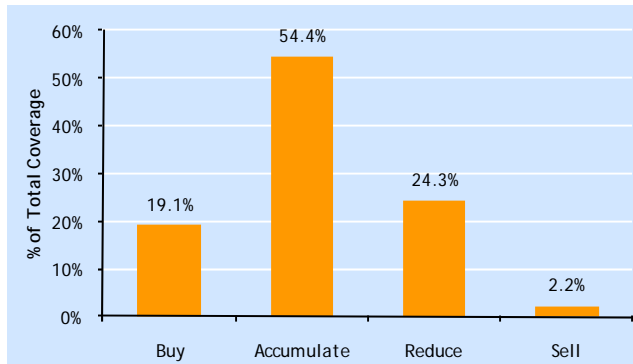
Source: Company Data, PL Research

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#### Rating Distribution of Research Coverage



#### PL's Recommendation Nomenclature

<b>BUY</b>	: Over 15% Outperformance to Sensex over 12-months	<b>Accumulate</b>	: Outperformance to Sensex over 12-months
<b>Reduce</b>	: Underperformance to Sensex over 12-months	<b>Sell</b>	: Over 15% underperformance to Sensex over 12-months
<b>Trading Buy</b>	: Over 10% absolute upside in 1-month	<b>Trading Sell</b>	: Over 10% absolute decline in 1-month
<b>Not Rated (NR)</b>	: No specific call on the stock	<b>Under Review (UR)</b>	: Rating likely to change shortly

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