

19-02-2017

CMP: 1878 Weight: 10%



STOCK DATA

Market Cap(Rs. cr)	32,358
EPS (Diluted) – 31 st Dec,16	54.55
P/E	29
P/B	2.61
Promoter’s Holding	51.44%
52 Week High/Low	2097/832.25
Shares Outstanding (in Cr.)	17.23

KEY FINANCIALS

(Rs. in cr)

Y/E MARCH	2013	2014	2015	2016
Revenue	3699	4724	5377	6852
Operating exp	3088	3864	4237	4738
EBITDA	611	860	1140	2114
Depreciation	210	247	290	327
Interest Expense	575	1049	511	939
Exp. Item	(19)	1	2696	46
PBT	(193)	(435)	3035	894
Taxes	25	63	345	103
PAT	(218)	(498)	2690	791

VALUATION – We believe the company can double its profit in the next 2-2.5 years, demerger will double the Market cap of the company from 32,000 crores to 57000-64000 Crores in next 2 year. The downside is limited to 20%, whereas upside we can expect large value unlocking post the demerger.

PIRAMAL ENTERPRISES LTD.

Thesis –

At Stallion Asset we have a consistent Philosophy of buying companies that can:

- 1) Grow at more than 25%
- 2) Huge Opportunity Size
- 3) High Return on Equity
- 4) Smart and Ethical Management

Piramal Enterprises fits into our criteria of growth at a Reasonable price, We expect the company double its profits from here on in next 2-2.5 years backed by Growth in AUM in Real Estate Financing, Turnaround in Pharma division and annuity from IT business.

Warren Buffet was once asked what are the first things you look for in management team? He Answered Intelligence, Energy and Integrity.

Mr. Ajay Piramal, the Chairman of the Pirmal is who we believe is an intelligent fanatic has an aggressive approach and is known for acquiring niche and potential businesses, turning them around and selling them at much higher value thus creating massive value for the shareholders.

Every Bull Market makes one person or company the Richest/Biggest.

1996-2000 – Technology bull Market made the Azim Premji (Wipro) and Infosys

2003-2007- Made Mukesh Ambani the richest person, Bharti(Airtel) the biggest telecom co.

2009-2014 –Made Dilip Sanghvi and TCS

2016-2020- Making of Maruti, Bajaj (Auto and Finance) and Piramal? A Possibility.

History of Piramal Group –

Phase I: 1988-2010 – In 1988, Ajay Piramal, Chairman of the company, moved out of the textiles business and acquired 48th rank Pharma company i.e. Nicholas Laboratories. He successfully transformed the company via organic and non-organic route and made it through top 3rd Pharma Company in India.

Phase II: 2010-2017 – In 2010, Company sold the domestic formulation business to Abbott for \$ 3.72 billion (Rs. 17,300 Cr) at 9x FY2010 Sales and 30x FY2010 EBITDA. The 2000 cr Sales domestic formulations business accounted for more than half of the healthcare revenue. It acquired I-Pill brand from Cipla for a consideration of 95 Cr and sold its diagnostics business to Super Religare Laboratories (SRL) for 600 Crores. SRL was a bad exit for Piramal as SRL is valued at 4,000 Crores today.

2011- Piramal Acquires 11% stake in Vodafone India in two tranches of 5.5% in August 2011 and February 2012 at an average of Rs. 1290 a share (5864 crores).

2012- It enters the financial services business as an NBFC with a focus on real estate lending.

- Acquires health care information management firm, Decision Resources Group, USA for USD 635 Million.
- Piramal Enterprises Limited acquires Molecular Imaging Development portfolio of Bayer Pharma.

2013 – Acquired 10% stake in Shriram Transport finance Corporation with an investment of 2156 Cr. Piramal Enterprises Ltd. consumer products' division acquires the brand CALADRYL in India.

2014- Acquired 20% stake in SCL for 2146 cr and 10% stake in Shriram city union finance for 801 cr. In November 2014, Ajay Piramal is appointed as a chairman of Shriram Capital.

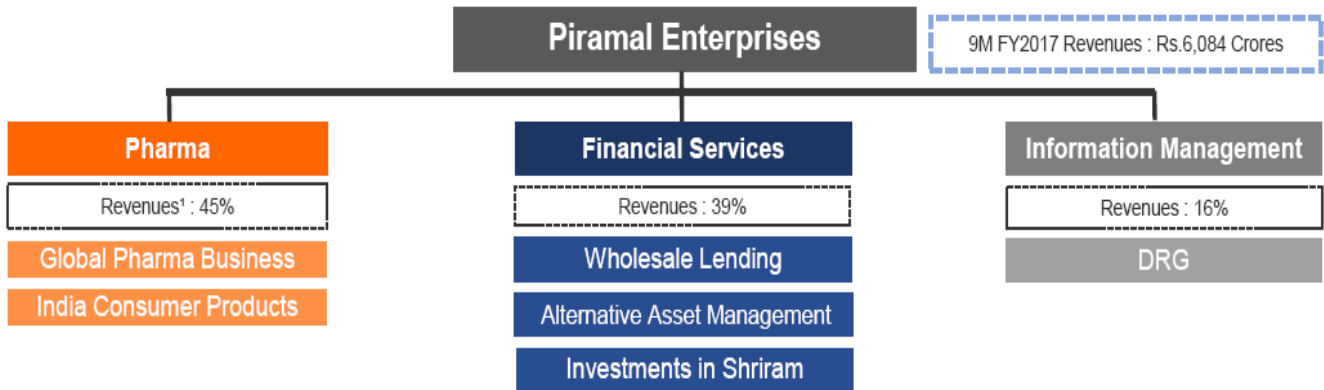
- Sold 11% Vodafone stake for 8,900 crore (Generated 19% IRR)
- Decision Resources Group acquired Relay Technology Management. The acquisition adds new products and significant technological capabilities.
- APG Asset Management, the Dutch pension fund asset manager and Piramal Enterprises Limited announce a strategic alliance for investing in rupee denominated mezzanine instruments issued by infrastructure companies in India with a target investment of US\$ 1 Billion over the next 3 years.

2015-2017- In last 2 years, PEL has done 7 acquisitions with a total investment of 3000 Cr.

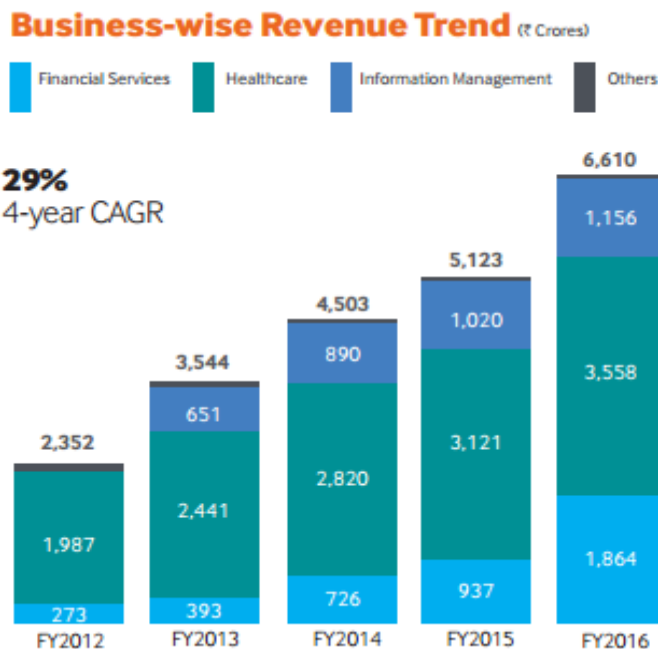
- Coldstream - Injectables
- Ash Stevens – HPAPI
- Injectable anaesthesia and pain management products (Janssen and Mallinckrodt).
- 4 brands from Pfizer Ltd. (110 cr.)
- 5 brands from Organon India and MSD BV
- Baby care Brand “Little’s”

In Jan 2017, Company has announced that they are going to enter the housing Finance space. DRG has acquired Healthcare Business Insights (HBI), a trusted provider of best practice research, training and services to more than 1,400 hospitals across the U.S.

Present Piramal Enterprises Limited



Piramal Enterprises Limited (PEL) is one of India's large conglomerates with its presence in three important segments namely Healthcare (45%), Financial Services (39%) and Information Management (16%) as on 9MFY17.



Since the company has operations in three different segments i.e. Healthcare, Finance Services and Information Management. We will discuss segment wise.

- 1) Healthcare Business:** Healthcare business was once a major revenue contributor (80% in FY11), now contributes 45% to the total PEL business with exports being the dominant part of the revenue. Company's pharma business includes Global Pharma and India Consumer Products.

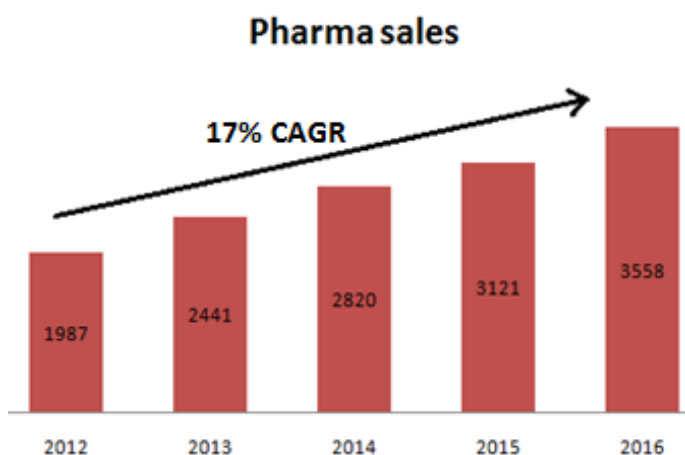
	Global Pharma Solutions	India Consumer Products
Revenue Mix	89% of the Pharma revenue	11% of the Pharma revenue
Products	Inhalation anaesthesia, API Generics, pain management, HPAPI	Saridon, I-pill, Lacto calamine, Littles
Niche	12% Global Market in Inhalation Anaesthesia in 2015, from 3% in 2009	Among top 10 OTC Players Most brands among the top 2 in their respective markets.
Ebitda Margin	21% (Proforma FY16)	Low single digits
5 year CAGR sales growth	18%	18%

We at Stallion Asset have been not every bullish on the pharma business because they have been treated as defensives stock when they are not due to US FDA risks. All Major pharma companies has been in stress due to pressure from the US FDA due to many inspections, surprise checks, notices to companies and due to such measures the business operations have come to standstill as well. Inspite of the FDA risk, in the last 5 years, this company has cleared all the inspections and audits:

- 24 USFDA inspections
- 43 other regulatory inspections
- 560 customer audits.

Piramal is one of the only Indian Company which has never faced FDA problems, clearly showing the level of governance they have maintained. This has increased our confidence in the company as far as pharma business in concerned. They are the third largest in anaesthesia segment with 12% market share and among top 10 in CRAMS in the world. The newly acquired OTC Products will support the growth as well.

Pharma Business Sales Growth – 17% 5 year CAGR



Company currently has revenue of 3558 Cr. and is expected to increase to 6500-7000 Cr. by 2020 (management projections) growing at 15%.

The company target to have EBITDA margin of 20-25% by FY 2020.

Understanding the Pharma Business and Valuation- Pharma Business can be divided in 4 Parts

1) Piramal Pharma Solutions – It is among the top ten CDMOs (Contract Development and Manufacturing Organisations) in the world. In FY16 the revenue in this segment grew at 14% on the back of traction in API and Formulations businesses. The revenues in this segment have grown from 885 Cr. (2010) to 2290 Cr. (2016).

Year	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
CRAMS	1021	1355	1553	1786	2008	2290

2) Piramal Critical Care – Company entered the Inhalation Anaesthetics business by acquiring pharma business of ICI India Ltd with revenues of less than 9 crores in 2005. Piramal has come a long way via organic as well as inorganic growth in this space to become the third largest player in the world with the market share of 12% and revenues of 876 Cr. Their continued focus on cost leadership and acquisitions will help them increase market share. They have a market share of 30% in USA which is the biggest market.

Year	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
Anaesthesia	388	413	616	720	757	876
Global Market Share has Increased from 3% in 2009 to 12% in 2016						

3) Consumer Products – Piramal owns strong consumer brand like Saridon, I-pill, Iaco Calamine. Piramal has expanded its consumer business from 481 cities in 2012 to 1500 today. It has presence is more than 4,00,000 outlet in India. Consumer division is a difficult division as there are pharma pricing problems in India, but the company had guided to be the third largest over the counter player in India by increasing sales to 1,000 crore by 2020.

Year	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16
Consumer Products	195	219	272	314	356	392
Rank	14	10	7	7	6	5

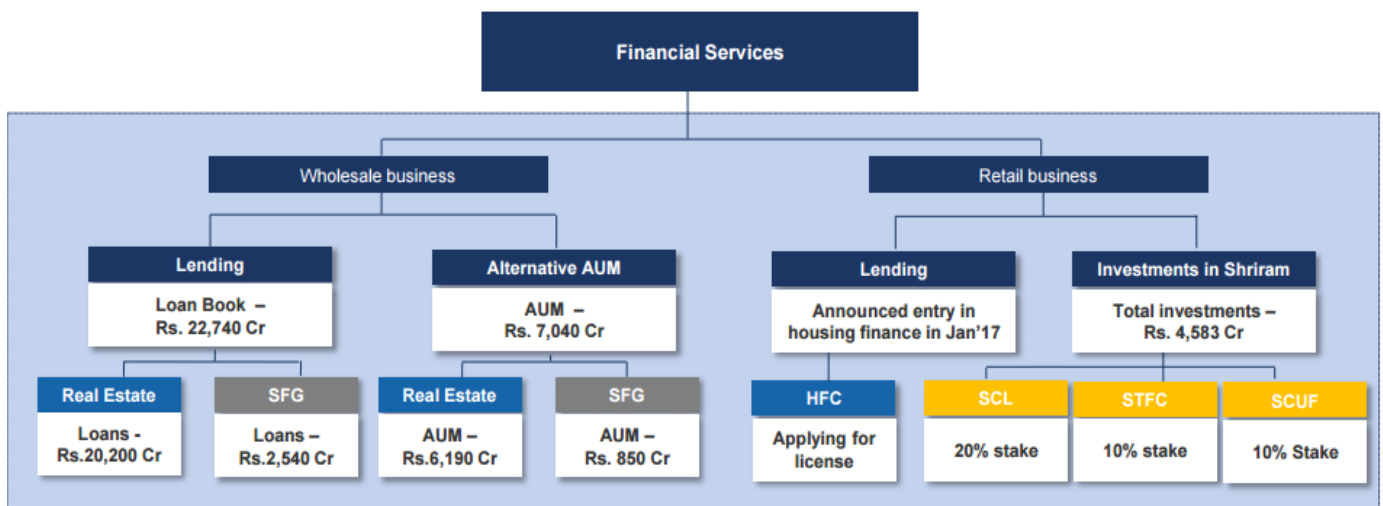
4) Imaging – Piramal Acquired bayers molecular imaging asset. It was acquired for 11.5 million dollar and piramal has incurred net loss of 254 Cr., 151 Cr. and 99 Cr. in FY 2016, 2015 and 2014 respectively. This was a drain to the profitability of Piramal. Ajay Piramal in his analyst concall has said no new investment will be made in this company after Q3 2017 and they might sell this subsidiary.

Plans for the Future and Valuation – The Company has guided for revenues of 6500-7000 Cr by 2020 and EBITDA margin of 20-25% i.e. approximately 1300-1750 Crores of EBITDA. They have done Proforma revenue of 4300crores in 2016. We believe the 6500-7000 Crores sales target is absolutely achievable and the Pharma business should be valued at atleast 10 x EV/EBITDA in FY2020 or 15,000Crores.

2016 Data (inr Crores)	Revenue	Margin	Enterprise Value	EBITDA	EV/EBITDA
Sun Pharmaceutical Industries Ltd	28,270	31%	1,56,791	8764	18
Dr.Reddy's Laboratories Ltd	15,698	26%	49,309	4081	12
Lupin Ltd	14,208	28%	73,502	3978	18
Aurobindo Pharma Ltd	13,896	23%	44,693	3196	14
Cipla Ltd	13,678	19%	52,554	2599	20
Cadila Healthcare Ltd	9,838	25%	39,794	2460	16
Glenmark Pharmaceuticals Ltd	7,560	19%	30,154	1436	21
PEL Pharma	6750	23%	NA	1519	NA
Divi's Laboratories Ltd	3,776	38%	18,797	1435	13

*PEL 2020 Data has been assumed

2) Financial Services – The financial Services space can be divided into 2 broad categories i.e. Wholesale Business and Retail Business. The Retail business is largely the acquisition of Shriram stake where have invested 4,800 cr. and now they have decided to enter the booming housing finance space. Wholesale Category is lending to Real Estate developers in various stages of construction? Sounds risky right, then what makes us so bullish on it.



Understanding Wholesale Lending Business - Piramal had total loan book size of 22,740 in December 2016, majority of it was given to real estate. We have been reading about the real estate lending division for last 4 months to understand who piramal does it so efficiently whereas bank can't.

What makes the Piramal's Quality so robust?

While we were doing a background check, we understood that banks are in no shape to lend to real estate builders due to their inability to collect loans but atleast 10-15 lakh crores of capital is required by builders in next 5 years. If a builder gets loans from Piramal that builder is considered AAA by the lending community because that's exactly how robust is piramal's credit quality test.

Highlights of Piramal's Real Estate lending

- Presence in Tier 1 cities only
- Grade A developer with good track record
- 10 years of experience in real estate market
- Structure deal uniquely whereas banks don't have that.
- Majority of team dedicated to monitoring of assets via monthly performance and reviews.

Why are we optimistic?

- Controlled NPAs
- Robust AUM growth in spite of demonetisation
- 25%+ ROE
- Mindblowing management team under Khushru Jijina

Present in all stages of real estate lending

Company has been very selective in lending real estate loans (construction finance forms majority). The strategy of the company is to lend to big and well known builders from tier 1 and metro cities which they think have the ability to repay their loans on time. Piramal has extremely manageable NPA levels at 0.55% (31st December, 2016).

	Current Size	Average Yield/IRR	Tenor	Comment
Mezzanine Lending	8940 Cr	17-19%	3-5 yrs	Phase between land Purchase and commencement of construction.
Construction Finance	11260 Cr	14-16%	4-6 yrs	Construction of Projects
Lease Rental Discounting	Started in 2016	11-12%	9-12 yrs	Target to scale up the book size to 10000 Cr by FY18

Valuation of Piramal Lending Business – We don't exactly know what is the book involved in Piramal's Real Estate lending division but our approximately calculations suggest that it is about 5,000 Crores. Majority of Home Finance companies including Gruh, DHFL etc are leveraged 10-13x, we believe Piramal will have reach a loan book of 50,000Crores by FY2019 and have an net of tax ROA of 3-3.4%.

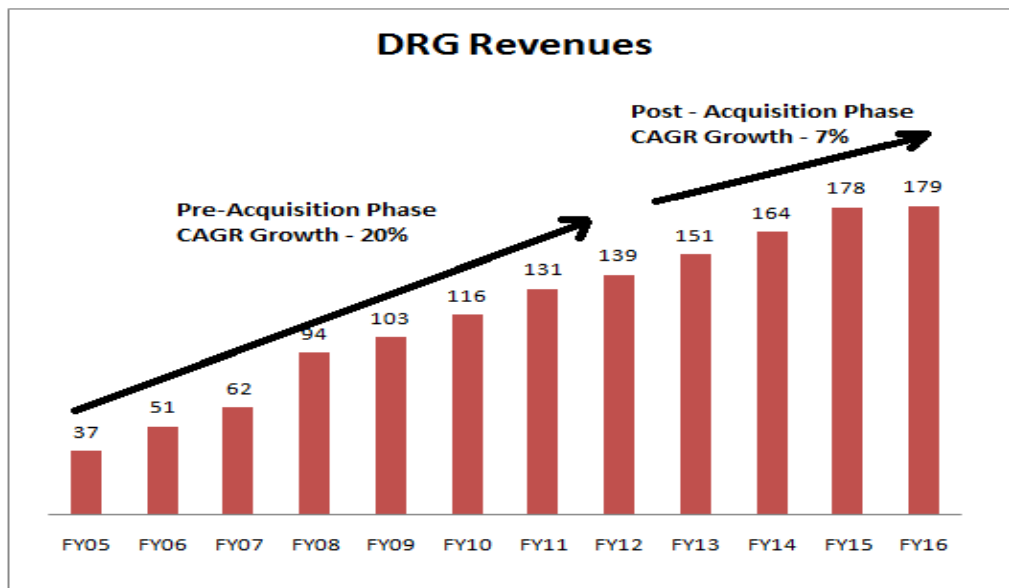
3) Information Management

Information Management segment of the company comprise of DRG(Decision Resource Group) which was acquired in the year 2012 for 3400 Crores at 4.5x Sales 2012 .DRG is into technology for Pharma companies wherein the revenue is divided into Data Analytics(43%),Research Products (35%) and Global Consulting (22%).

Client for DRG includes majority of top 50 pharma companies globally. The company has 75% of revenues recurring in nature and has a 97% customer retention ratio.

DRG has acquired two companies HBI and adaptive software which has increased the opportunity size for the company. DRG has grown slower than initially expected by piramal, nonetheless they are planning to shift jobs from USA to india to reduce cost and have opened offices in Bangalore and Gurugram.

DRG Growth has slowed post acquisition. We continue to believe that DRG will at 7% in dollar terms whereas the INR will depreciate 3-4% YOY, we assume a 10% growth in INR terms for DRG.



Valuation of Piramal Information Management Business –

\$ Million TTM	Sales	Market Cap	Mcap/Sales
Veeva System	508	6100	11
Verisk	1995	14000	6
Medidata	438	3200	6
Athena	1083	4500	3
DRG	180	720	4x Sales Est.

When we do a relative valuation of DRG will peers, we understand the DRG if listed today in American markets would have a market cap of between 700million USD to 1 Billion USD.

Valuation of the combined entity in 2019 – Our Estimates suggest that the demerger Piramal Entity will be value at 57000-64000 Crores against 32,000 crores today. According to our understanding there will be limited downside from these levels and a high probability of this stock giving 100% returns in next 2 years as demerger happens.

FY 2019 Expectations	Comment
Financial Service	Profit of 1500-1800 Crores and Valued at 20 PE = 30,000-36000 Crores
Pharma Division	Valued at 10x EV/EBITDA of FY 2020 at around 15000 Crores
DRG	Valued at 4x expected sales of 220 Million = 880 Million or 6000 Crores
Shriram Group	$6000 * 1.12 * 1.12 = 7500$

The promoter was buying aggressively around 1500 levels when the markets corrected due to demonetization. Ajay piramal is a great guy to partner our investments with.

Conclusion -

Piramal Enterprises plans to lists its two entities i.e. Healthcare and Financial Services separately in next 18 months to unlock value for its shareholders. DRG part of Information Management Business will be spun off and listed separately in U.S. Whenever the demerger happens, be it 2018 or 2019 there will be huge value unlocking for shareholders. At current juncture Piramal trades at 25 Times FY2017 Earnings and 10-11x FY 2019 years. By FY2019 we believe the return on equity of the combined entity will be close to 20% and expected growth rate then would be 15-17% CAGR. In 2019 Piramal should as per our estimates trade at a market cap of 60,000 crores plus if demerged. As on today we have limited downside risk as we believe that demonetization low won't be broken whereas upside is 100% in 2 years.

Analyst Position- Amit Jeswani and Family have no Positions.

Juhi Shah-no positions

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