INSTITUTIONAL EQUITY RESEARCH

Agri Conference

Key takeaways

INDIA | SECTOR UPDATE

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We organised an **'Agri Conference** on 12th January 2017 in Mumbai. In this day-long event, we hosted the following luminaries for panel discussion and board room meetings.

Boardroom meeting participants

- ✓ Agri Business and Commodity Market Specialist
- ✓ NEML (National Electronic Markets Ltd.)
- ✓ Insecticides India
- ✓ ED&F Man India (Sugar Expert)
- ✓ Savannah Seeds (Rice)
- ✓ Maiia Commodity Management Pvt Ltd
- ✓ KRBL
- ✓ Agriculture Policy Expert
- ✓ White Organic Agro

Panel Discussion Key Takeaways

- India is third largest agri producer after China and USA with ~15% GDP contribution. India has ~16% of world population supported by less than 3% of land resources and 4% water resources. Limited resource in land and water with growing demand present opportunities in agri value chain.
- India has sustainable drivers for growth over next 20 to 25 years with growing demand, rising income and current very low consumption level. The government is focusing on agriculture for job led growth as 50% of population depends on it.
- Total land cultivation is ~140mn Hectare (Ha) with two cropping in a year. The crop intensity in India is significantly lower at 1.3x compared to ideal intensity estimated at 1.8x. The potential increase in land intensity will substantially increase demand for fertilizer and agri inputs.
- Need to increase land usage with investment in irrigation to expand acreage. Around 3mn ha land is expected to bring under irrigation over next two years. Total 100 projects are under implementation to bring 7.6mn Ha land under irrigation with investment of ~RS 8.5tn.
- Tropical climate in India need more heat and climate changes resistant crop verities. Wheat and Maize has reached to heat tolerant level and India needs to develop new verities for yield improvement.
- Incentives are required for PPP in agriculture to double farmer income, encourage high value crop and integration of supply chain from off-takers to farmers. Value creation opportunities for private players are in pesticide and seed in upstream side and consumer facing distribution through brand creation on downstream side.

- Significant shortage in agri warehousing capacity in India. Currently ~1300 warehouses are registered with total storage capacity of 6mn tonnes and ~439 are used by commodity exchange for storage. Food Corporation of India (FCI) has ~35.8mn tonnes own storage and 46.7mn tonnes hired storage capacity. More investment from private players is expected with investment opportunity of USD 5bn.
- Electronic platform for mandis shifted manual transactions and auctions form to electronic mode and has improved transparency. However their success is limited due to non availability of integrated service providers for grading of products, transportation and credit availability
- Fertilizer subsidy is expected to remain at same level with elections coming in many states. The government is working on reducing cost of manufacturing in Urea by setting up plant close to raw material availability and reducing the slippage of subsidies. The direct benefit transfer (DBT) to farmers will require micro planning and will require long time to do it. The fertilizer subsides will continue to be given to fertilizer companies instead of farmers based on sales receipt. Currently urea prices are subsidies by ~70% and farmers will find difficulty to pay full money upfront in case of DBT with lack of credit. Another issue with DBT is 30-40% hidden tenancy on agricultural land and need land reforms to make it successful.

- Industry also facing shortage of cold chain network and provide investment opportunity of ~5-6bn in reefer logistics and transport.
- De-monetization impact was much higher on perishable side and expect commodity price to remain soft with higher output this year.
- Crop insurance policy is good and ~40-50% farmer are benefiting from it. However current insurance premium of ~18% are not sustainable (subsidized rate for farmer is 2% on kharib and 1.5% Rabi).
- IT revolution has bypassed agriculture in past ten years and now it can be implemented aggressively in agri sector with web based solution to connect farmers with off takers.
- Inconsistent polices in sugar has impacted growth in Sugar sector over past years and expect lower production of ~21mn in current sugar season. Industry is expected to import 1-2mn tonnes sugar to meet the shortage and demand supply mismatch is expected to keep sugar prices up.

KRBL

- The company is largest producer and exporter of branded basmati rice. It holds ~25% market share in branded Basmati exports from India. It is market leader in domestic branded market with ~35% market share followed by Dawat ~15% and Kohinoor ~10%. In rice segment branded players control ~40% market while un branded market is 60%.
- Basmati Rice is just 2% of total Rice Production in the World and it is grown only in India (70%) and Pakistan (30%). “India Gate”, the flagship brand of Company, is the topmost selling rice in the Branded Rice segment, both in India and Overseas market.
- Rice manufacturing capacities of 195 MT per hour. Export price per MT commands a premium of more than 30% over the Industry average.
- Wide marketing network with presence at 6,72,000 retail outlets spread over all towns and cities of the Country. Being an integrated player, the Company generates value-added by-products like brain oil, de-oiled cakes and uses rice husks for captive power plant.
- Benefit from huge storage system and do a 3-step check on the paddy seeds when they are with the buyers, again at Mandi and later at the Godowns. Keep stock of 2-3yrs old basmati rice in their inventory which are ready for sale.
- The payment is done to the farmers within 7days, and the firm avails 2% discount at the cost for the same. The payments are done by cheques (100%), hence no adverse impact from demonetization. They try to retain their farmer`s base of paddy, by doing some CSR activities. The CSR activities includes, try to educate farmers about the new techniques in farming, seminars on the good crop and seeds verification, etc.
- The company has 500 dealer base, that covers around 5 lakh retail shops. The price of paddy has come down to Rs 17-18, from Rs 23 in 2016, the company is planning to keep the prices stable at Rs 70/kg, because of lowering cost of inputs. In their exports, 70% of their revenue comes from the middle east countries. In the domestic markets, south India accounts the highest revenue of 30-35%, followed by north India (20-25%) and west (20-23%) and the rest is north east states.
- The payment is done to farmers within 7 days and gets 2% discount for it. The payment is 100% by cheque, hence no adverse impact of de-monetization. Developed strong relationship with farmers (also supported by CSR) and educate farmers about new techniques in farming, arrange seminars etc.
- Company is planning to extend its operations into the rice-bran oil sector (currently they are selling it to Saffola as raw material) and already have started operations in the brown rice segment (targeting the health conscious population).

MAIIA Commodity

- Founded by de Souza family in 2010, MAIIA has now grown into one of the most efficient Collateral Management services company in the country covering 11 states of North, West & South India, and continues to expand rapidly into more & more territories.
- Its services range also includes Stock Monitoring Assignments, Inspection & Testing Services, Certification & Verification Services, and other customized service needs for Indian & International Banks, Financial institutions as well as Corporates dealing in agricultural commodities
- The company started their business, by charging Rs.5-7/sq feet in their warehouses, which gradually increased to Rs.30/sq feet. The key commodities that they store are grains, pulses, oilseeds, complex spices, cotton, sugar, jiggery and non-ferrous metals as well. The capacity utilization of the warehouse space is 70%.
- It also provides cold storage and liquid storage as per the needs of the clients. They also charge for warehousing fees, collateral fees, loading and unloading fees. Liability for the business comes into picture only when the goods of the customers are damaged, for that they keep it insured beforehand.
- Volatility in commodity prices affects positively to the business because clients will go long and store their products for a longer period of time. There is no major default risk (as they follow the advance rent policy) in this business, the environment got critical due to demonetization, but no major setbacks. There can be around 1% risk of default, but they are already insured for the same.

White Organics (earlier White Diamond Industries)

- The company is first listed entity catering to entire organic product range. It has 160 Premium Organic products in 12 major categories and 17 sub categories.
- The company has strong presence of own farmer base of ~108 acre through lease model mainly in Gujarat. It is targeting to increase organic farm acreage to 1200 over next 12-18 month with focus on quality assurance at every step of processes.
- It is also developing retail business through owned, franchise, e-com and exports. It has opened one retail outlet in Central Mumbai and Targeting 15 stores in next 3 years along with additional 30 retrial outlets through franchise model.
- The company is targeting huge demand for healthy and nutritious food product amongst health conscious people. Indian organic food market is expected to report CAGR of 25-30%.

NEML (National Electronic Markets Ltd.)

- NeML is a wholly owned subsidiary of NCDEX, India's largest Agricultural commodity exchange with more than 90% market share. It works with domain experts and offers trading platforms for trading in a host of commodities, both agricultural and non-agricultural to various market participants, primary producers including farmers, traders, processors etc. These trading platforms combine technological efficiency and market friendly trading features in a transparent atmosphere to make trading a rich and rewarding experience.
- In 2014, Karnataka took the mandi (farmers' market) system to the virtual world with setting up Rashtriya e Market Services Private Limited (ReMS) as a joint venture between the state government and NeML. As of March 2016, ReMS had integrated online 105 of the 155 APMCs across 27 of the 30 districts in Karnataka through a single licensing system. This has created what the state calls a unified market platform (UMP).
- Management sees a shift from cash to cashless transaction at the Mandi level and which will help in transparency at Mandi transactions. However, there are

few challenges like (1) strong resistance from trader side (the mandies are dominated by the traders) and (2) Transaction process from Mandi is to directly deposits amount in farmer's account but the farmers are more depend on cash transactions for farming related buying, logistics and others costs.

- Crop loans will help farmers in big way by providing financial support in farming as well as it also gives insurance to farming related risks. Crop loans are generally disbursed by the banks through the mode of Kisan Credit Card (KCC). All farmers including small farmers, marginal farmers, share croppers, oral lessees and tenant farmers are eligible for issuance of KCC. KCC holders are also covered under Personal Accident Insurance Scheme (PAIS) against accidental death/permanent disability.
- The electronic National Agriculture Market (e-NAM) has covered over 250 markets. However, most of them are at a nascent stage and grappling with operational issues. e-NAM operations includes (1) Quality testing centre at the mandies, (2) Automation of auction process to bring transparency and ease of doing business for farmers, (3) provides funding requirements, (4) Information technology support at the Mandi etc.
- Company believes in remote buying in India as it will help in reducing logistic costs, goods wastage, physical handing by farmers etc. However, he feels India is much behind in implement remote buying.
- Government operates through its MSP centers and it opens window for 10-15 days at selective centers only. However, through these MSP centers government generally incurred loss as buying is always at higher price and selling at lower price due to demand driven pricing. He highlighted two major challenges at MSP centers (1) Multiple round of buying and (2) Substandard quality. However, management feels MSP is only a physiological support to the farmer.
- Central government does not participate in contract farming as it is done at state level only. The three elements in it are (1) Sponsor, (2) Producer (farmer) and (3) agreement.

Insecticides (India) Limited (IIL)

- Insecticides (India) Limited (IIL) is amongst the top 10 Indian agrochemical companies having approx. 7% market share of the Indian domestic agrochemical market.
- The company has a fully integrated business model right from manufacturing of technical and branded formulations to sale of generic and in-licensed agrochemical products. IIL has a pan India presence with network of 5000 plus distributors and 29 depots and branches. It has 5 Formulations & 2 Technical facilities at Chopanki (Rajasthan), Samba (J&K), Udhampur (J&K) and Dahej (Gujarat). IIL indicates to have average utilization level of 60% across all plants.
- The company has a portfolio of strong & successful brands which includes 9 brands under Navratna category (inlicensed, leased or own brand) and 11 brands under super 11 category (mostly reverse engineering) contributing 52% and 13% of its total branded formulations sales in FY15 respectively. It has International tie-ups with AMVAC and Nissan Chemicals (through Nagarjuna Agrichem Ltd.), for brand licensing and marketing rights.
- The company intends to further move up in the value chain by developing new molecules and has set up an R&D centre through a JV with OAT Agrio, Japan. The company indicates for have more number of such tie-ups going forward.
- IIL is focusing more on its R&D activities and has identified 20-22 products and as part of its short term growth strategy, it intend to add one product every year through reverse engineering of off patented molecule (life of the product is approx. 2-3 years) as well as one co-licensing product.
- IIL has strong brands present across all types of pesticides. Insecticides contribute 60% of the sales followed by Herbicides 23% and Fungicides 11%. The

branded business contributes ~77% of its sales and the balance is institutional sales.

- IIL recently launched a new post-emergence herbicide Green Label, manufactured in India for the first time using advanced technology. Green Label contains active ingredient bispyribac sodium 10% SC, which is a broad spectrum systemic herbicide. It indicates to have 15% market share in the product so far. Other companies like PI Industries and Garda chemicals are the key competitor for this product.
- IIL indicates to focus more on international business with geographical expansion. It guides Rs 1bn export sales in near future from current level of Rs 230mn.
- It indicates to face difficulties in registration of products in international market due to continuously strengthening of norms from global regulatory bodies.
- IIL expects its top 20 products will contribute ~75% of sales in near future which will drive the value growth for the company.
- China agrochemical companies facing plant shutdown or plant relocation issues to match up the environmental norms of China. IIL sees incremental opportunity from these China slowdown.
- The company's revenue, EBITDA and PAT has grown at a CAGR of 17%, 16% and 4% respectively in FY11-16. It guides for sustainable sales growth with EBITDA margins expansion to 14-14.5% in FY18 from current level of 10.5%.

Savannah Seeds

- Savannah Seeds is the subsidiary of large European Conglomerate and is expert in rice and largest rice seeds companies in the world. It is present in 13 states and further expanding its presence in Vietnam in next 2-3 months.
- Perishable crops were impacted more compared to other crops due to demonetization, however winter sowing was surprisingly good.
- 90% use labor for transplanting and surprisingly total cost for transplanting is $4bn.
- 98% of rice is used as a food crop and rest is used in alcohol and various other industries.
- Concerns like milling process, taste, long rice has discouraged the customers and millers in using hybrid rice. However, newer hybrid rice version has shown some interest to customers. Newer hybrid rice takes 5-6 years for development.
- Farmers are ok of using generic agro chemicals; however when it comes to seeds, they strongly prefer branded seeds only.
- MNC controls 60% of the total seeds market, led by Monsanto and Bayers
- As per Indian food regulations farmers cannot use BT-GMO seeds in food seeds except cotton.
- Corn is the fastest growing hybrid crop which now accounts for 80-90% of total corn crop.

Rating Methodology

We rate stock on absolute return basis. Our target price for the stocks has an investment horizon of one year.

Rating	Criteria	Definition
BUY	>= +15%	Target price is equal to or more than 15% of current market price
NEUTRAL	-15% > to < +15%	Target price is less than +15% but more than -15%
SELL	<= -15%	Target price is less than or equal to -15%.

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