

2nd August 2007

Ballarpur Industries

Event
Update

Unlocking value – great potential upside

Buy

Price	Target Price
Rs 132	Rs161
Sensex	14,936

Price Performance

(%)	1M	3M	6M	12M
Absolute	12	13	5	22
Rel. to Sensex	10	5	(1)	(12)

Source: Bloomberg

Stock Details

Sector	Paper
Reuters	BILT.BO
Bloomberg	BILT@IN
Equity Capital (Rs mn)	1857
Face Value (Rs)	10
52 Week H/L (Rs)	139/96
Market Cap (Rs bn)	24.5
Daily Avg Volume (No of shares)	636720
Daily Avg Turnover (US\$ mn)	1.9

Shareholding Pattern (%)

(30th Jun '07)

Promoters	38.9
FII/NRI	27.7
Institutions	22.5
Private Corp.	3.6
Public	7.4

Source: Capitaline

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Reorganisation exercise is to unlock value for existing shareholders. As per the guidance given by the management, we believe that the stock has significant potential upside of approx 56% to 122% from current levels with potential price target of Rs 204- 291. We reiterate our 'BUY' recommendation on the stock and however maintain our earlier price target of Rs 161.

BPH is likely to be valued at double the BILT's existing valuations

BILT is likely to place about 23-25% stake in BILT Paper Holding (BPH) and is likely to attract valuations of 11-13x EV / EBITDA while at present BILT commands EV/ EBITDA of 5.6x in domestic market on FY08 estimates.

Valuations comparable with global peers

The valuations looks aggressive if compared with domestic valuations, but they are in line with global valuations. Global pulp and paper companies generally command EV/ EBITDA multiple of 9-14x and P/E multiple of 15-20x (please refer to chart on page 4).

Why BILT should command global valuations

We believe that BILT is no more a domestic player after the acquisition of Sabah Forest (SFI) in Malaysia. BILT also have valuable forest inventory, which will take care of its fiber (raw material) requirement in long term. On business front BILT is now a fully integrated player starting from wood (forest resources) to captive pulp including captive power plant to paper and to high end retail stationery products including tissue paper. BILT has strong product portfolio which includes coated paper, copier paper, maplitho, creamwove while it has strong presence in branded retail segment through 'BILT' brand.

BILT offers better growth opportunities compared to global players

Consumption growth in India is expected to be 10-12% in line with economic growth, which is second highest growing market after the China. As on one side, we believe that the BILT should command premium valuations over to global players because of strong growth opportunities, better profitability and returns while on the flip side it is trading at significant discount of approx 50% to global peers.

BILT is poised for strong case of re-rating

We believe that there is strong case of re-rating and planned reorganization exercise by the company will give better comparable valuations. On the basis of BPH valuations, we believe that BILT has a potential upside of 56%-122% based on potential target price in range of Rs 204-291. For the potential target price, we have worked on two scenarios (please refer to table – scenario analysis on page - 2) and guidance given by the management.

We reiterate our 'BUY' recommendation on the stock; however we maintain our current price target of Rs 161 for the company and may revise the same after more clarity on this development.

Risks and concerns

However weather the company will be able to attract the private equity players at the price and valuations which the management has guided remain our key concern. The deal is subject to high court approval and is expected to be completed by Dec'07. Our potential target price is based on this particular event.

Business reorganization for significant value unlocking

We believe that BILT's reorganization exercise will unlock the value for its shareholders and should indicate potential true value of the company. As per guidance given by the management, we believe that the valuations which BILT commands in domestic market presently are at significant discount (almost 50% discount) compared with the one which it is likely to attract from private equity players through divesting some part (23-25%) of its existing business.

Scenario analysis for potential price discovery

On the basis of recent deal, and as per guidance given by the management we have done a scenario analysis to arrive at potential price target for the company.

Basic Assumption

- All the working is based on FY08 estimates while the reorganization plan, if approved by the honorable high court and as per guidance given by the management, is likely to be effective for FY09.
- We expect an EBITDA of Rs 2.8 bn from BGPPL and Rs 1.4 bn from Sabah resulting in total EBITDA of Rs 4.2 bn from BPH.
- Current debt on BPH (Sabah Forest) is Rs 4 bn (US\$ 100 mn) while approx Rs 4 bn (US\$ 100 mn) have yet to be taken (in next 12 months) as a part of Sabah acquisition deal. We have assumed current total debt of Rs 8 bn (US\$ 200 mn) on BPH for the purpose of valuation.
- We expect an EBITDA from BILT (residual business three plants and stationery products) of Rs 3.3 bn in FY08.

Scenario analysis	Scenario # 1(Optimistic)	Scenario # 1(Pessimistic)
	Placement for Rs 8 bn for 23%	Placement for Rs 6 bn for 25%
Rs bn	23%	25%
BPH Market cap	35	24
Total Debt	19.5	21.5
EV	54	46
EBITDA	4.2	4.2
EV / EBITDA	12.9	10.8
BILT consolidated		
BILT - EBITDA	3.3	3.3
EV / EBITDA (x)	6.0	6.0
BILT Target EV	20	20
BPH - EBITDA	4	4
EV / EBITDA (x)	12.9	10.8
BPH Target EV	54	46
BILT - cons EV	61	54
Buyback	9.0	9.0
BILT -cons EV net of Buyback	52	45
Net Debt	20.0	22.0
Target Mcap	32	23
BILT no of equity shares	1.1	1.1
Target Price- BILT	291	204
Potential upside	122%	56%

Source- Company, Emkay research

Potential upside of 56-122% from current Rs 132

In most optimistic scenario (given by the management) we believe that BILT's stock price has potential upside of 122% from current level while in most pessimistic scenario the potential upside is 56% with price target of Rs 204 and Rs 291, respectively.

How we have arrived at potential target price?

- Depending upon the case, we have calculated EV of BPH as per valuations given by the private equity players
- For valuation of BILT consolidated we have taken 77% (scenario 1) / 75% (scenario 2) EV of BPH plus BILT's EV (based on EV/EBITDA of 6x as per domestic valuation).
- Consolidated EV then further adjusted for buy back of 40% of current equity capital of BILT for a sum of approx Rs 9 bn.
- We have then subtracted net debt of consolidated BILT (Rs 20 bn in scenario 1 and Rs 22 bn in scenario 2) to arrive the target market cap of BILT consolidated.
- Target potential price then is calculated on the reduced equity (post buy back) of Rs 1.1 bn).

Scenario 1 (Optimistic) – Potential upside of 122% with expected price of Rs 291

Under the optimistic scenario we assume that the management is likely to raise a sum of Rs 8 bn through 23% stake sale in BPH and hence market value of BPH Rs 35 bn. Under this scenario, Total Debt on the BPH should be Rs 20 bn, as a result EV works out to be Rs 54 bn. At this price BPH is valued at EV/EBITDA of 12.9x for expected FY08 EBITDA of Rs 4.2 bn.

BILT's consolidated market cap (net of buy back) works out to be Rs 32 bn and per share price of Rs 291, which is 122% upside from current level.

Scenario 2 (pessimistic) – Potential upside of 56% with expected price of Rs 204

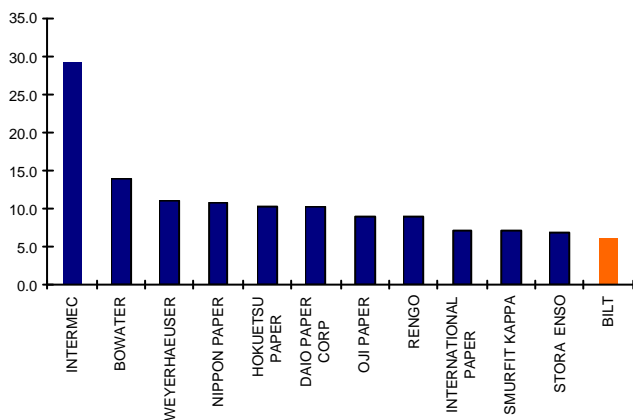
Similar to scenario 1, under the pessimistic case, we assume that the management is likely to raise a sum of Rs 6 bn from 25% stake sale in BPH and hence market value of BPH Rs 24 bn. Total debt of Rs 21.5 bn resulting in EV of Rs 46 bn and EV/EBITDA multiple of 10.8x.

BILT's consolidated market cap (net of buy back) works out to be Rs 23 bn and per share price of Rs 204, which is 56% upside from current level.

Reality check – valuations comparable with global peers

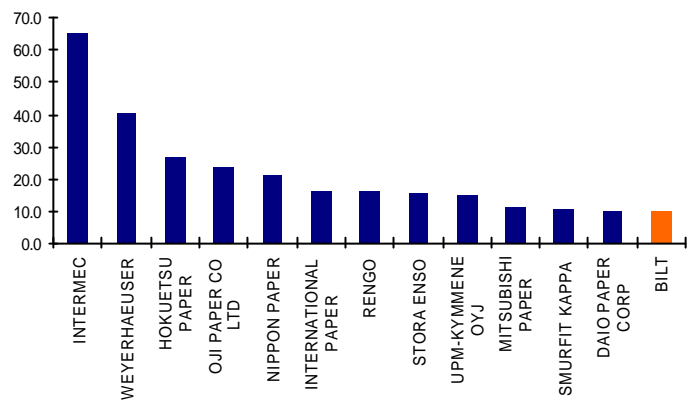
We believe that the management is talking about some aggressive valuations like EV/EBITDA of 10-13x which they are planning to get from the private equity players. However if we compare the same with the valuations what global paper companies command then the valuations look reasonable. Given the fact that BILT is not only the largest paper manufacturer in India but also has a sizable plant with rich forest resources through Sabah Forest (SFI), Malaysia. Also the growth in India market is attractive compared to any other country and per capita consumption of paper is still very poor and we believe that the consumption growth should be 10-12% pa on back of strong economic growth. We believe that BILT is very strong case of re-rating on the basis of global comparisons .

EV/ EBITDA multiple – global (x)



Source: Bloomberg, Emkay Research

P / E multiple - global (x)



Source: Bloomberg, Emkay Research

Risks and concerns

For the purpose of valuation and arriving at potential target price, we have taken guidance given by the management. Management however has not disclosed any information about the potential private equity players and concrete valuations at which money in BILT through BPH

Global comparison - Key financials and growth

US\$ mn	Net sales		EBITDA		PAT		Growth (%) 2008Y	
	2007Y	2008Y	2007Y	2008Y	2007Y	2008Y	Net sales	PAT
BILT	550	570	137	145	61	66	3.6	7.4
BOWATER	3221	3344	242	391	-154	-76	3.8	-51.0
CANFOR	3291	3457	-32	157	-142	-35	5.1	-75.1
DAIO PAPER	3460	3577	405	429	92	36	3.4	-61.2
HOKUETSU PAPER	1318	1414	166	185	41	45	7.3	10.4
INTERMEC	840	922	51	91	24	54	9.8	124.6
INTERNATIONAL PAPER	21562	22238	2904	3136	1019	1115	3.1	9.4
MITSUBISHI PAPER	2004	2131	-	189	62	41	6.4	-33.1
NIPPON PAPER	9834	10235	932	966	156	125	4.1	-20.2
OJI PAPER	10639	10904	1242	1190	207	201	2.5	-3.0
RENGO	3459	3603	339	357	90	74	4.2	-18.2
SMURFIT KAPPA	10246	10788	1540	1721	448	659	5.3	47.2
STORA ENSO	20929	21510	2895	3113	889	1064	2.8	19.7
UPM-KYMMENE OYJ	13925	14381	2469	2759	837	993	3.3	18.6
WEYERHAEUSER	16758	17231	2033	2236	450	641	2.8	42.3

Global comparison - Key margins and valuations

	EBITDA %		PAT %		P/E (x)		EV / EBITDA (x)	
	2007Y	2008Y	2007Y	2008Y	2007Y	2008Y	2007Y	2008Y
BILT	24.9	25.5	11.1	11.5	10.1	9.3	6.0	5.7
BOWATER	7.5	11.7	-4.8	-2.3	-	-	13.9	8.6
CANFOR	-1.0	4.5	-4.3	-1.0	-	-	-	13.5
DAIO PAPER	11.7	12.0	2.7	1.0	10.0	26.1	10.2	9.7
HOKUETSU PAPER	12.6	13.1	3.1	3.2	26.7	24.5	10.4	9.3
INTERMEC	6.0	9.9	2.9	5.9	65.4	29.0	29.2	16.2
INTERNATIONAL PAPER	13.5	14.1	4.7	5.0	16.2	13.4	7.2	6.7
MITSUBISHI PAPER	-	8.9	3.1	1.9	11.2	18.9	-	10.8
NIPPON PAPER	9.5	9.4	1.6	1.2	20.8	26.7	10.8	10.4
OJI PAPER	11.7	10.9	1.9	1.8	23.3	23.6	9.0	9.4
RENGO	9.8	9.9	2.6	2.0	15.8	19.0	9.0	8.6
SMURFIT KAPPA	15.0	16.0	4.4	6.1	10.4	7.6	7.2	6.4
STORA ENSO	13.8	14.5	4.2	4.9	15.7	13.0	7.0	6.5
UPM-KYMMENE OYJ	17.7	19.2	6.0	6.9	14.8	12.2	-	-
WEYERHAEUSER	12.1	13.0	2.7	3.7	40.0	27.5	11.0	10.0

Source: Bloomberg, Emkay Research

Business reorganization exercise

Ballarpur Industries (BILT) has proposed for reorganization plan which includes –

- BILT to transfer three out of six units in a separate company to be named as BILT Graphic Paper Products (BGPPL) for a consideration of Rs 19.5 bn in slump exchange.
- Later on Bilt Paper Holding (BPH), which currently holds 98% in Sabah forest, Malaysia, will also hold 100% in BGPPL.
- To fund Rs 19.5 bn, BPH is likely to raise a sum of approx Rs 6-8 bn through private equity placement for stake sale of 23-25% and rest Rs 12-13 bn through debts.
- BILT has plans for compulsory universal buyback for 40% of the equity share capital at price of Rs 125 per share. It has also proposed stock split in 1:5 (from Rs 10/- paid up to Rs 2/- paid up).

As per reorganization exercise, BILT's three unit – Bhigwan (installed capacity 115 thousand mt), Ballarpur (135 thousand mt) and unit Kamlapuram (Rayon grade pulp unit with capacity of 100 thousand mt) will be taken for slump exchange by company's wholly owned subsidiary (WOS) named BILT graphic Paper Products (BGPPL) at a lump sum value of Rs 19.5 bn.

BILT will continue to retain rest three units – Shree gopal (capacity of 85 thousand mt), Unit Sewa (72 thousand mt) and unit Ashti (55 thousand mt) which contributes approx 45% to the total paper capacity.

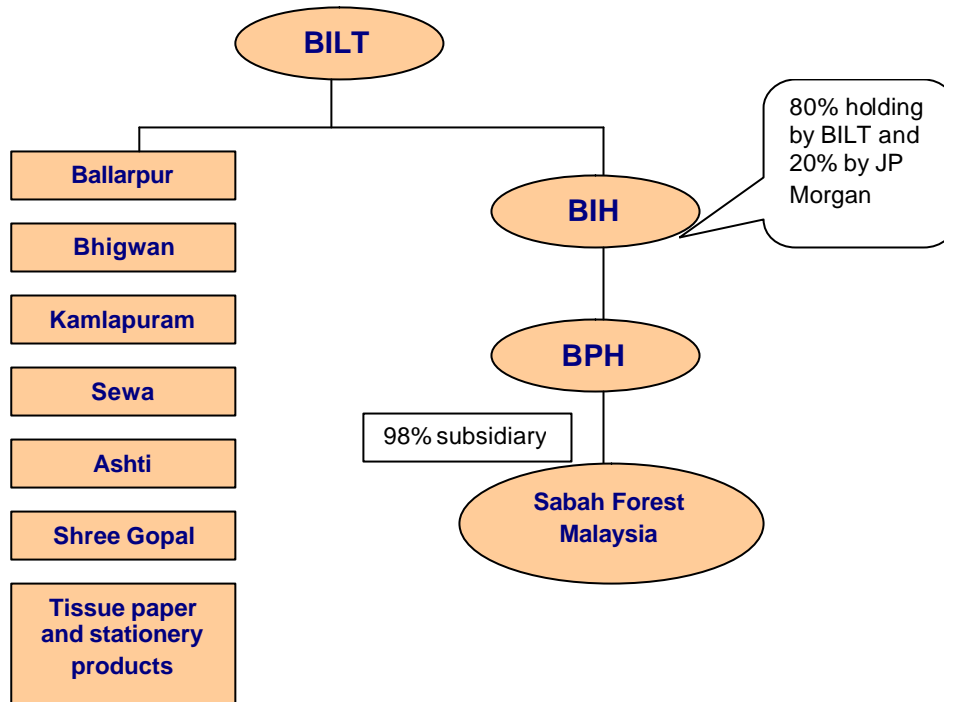
BILT has further plans to raise a sum of Rs 19.5 bn through debts / equity financing in its another subsidiary company – Bilt Paper Holding (BPH) which holds 98% stake in Sabah Forest, Malaysia (SFI). SFI is the Malaysian company which BILT recently acquired and the company was valued at approx Rs 12 bn.

The sum raised will be paid to BGPPL and from BGPPL to BILT, where it will be utilized to pay for the buyback (approx Rs 9.5 bn) and rest (Rs 10 bn) to repay the debt on BILT's balance sheet (current debt on BILT's balance sheet is approx Rs 14 bn).

Buyback – will not affect share holder's interest in the company

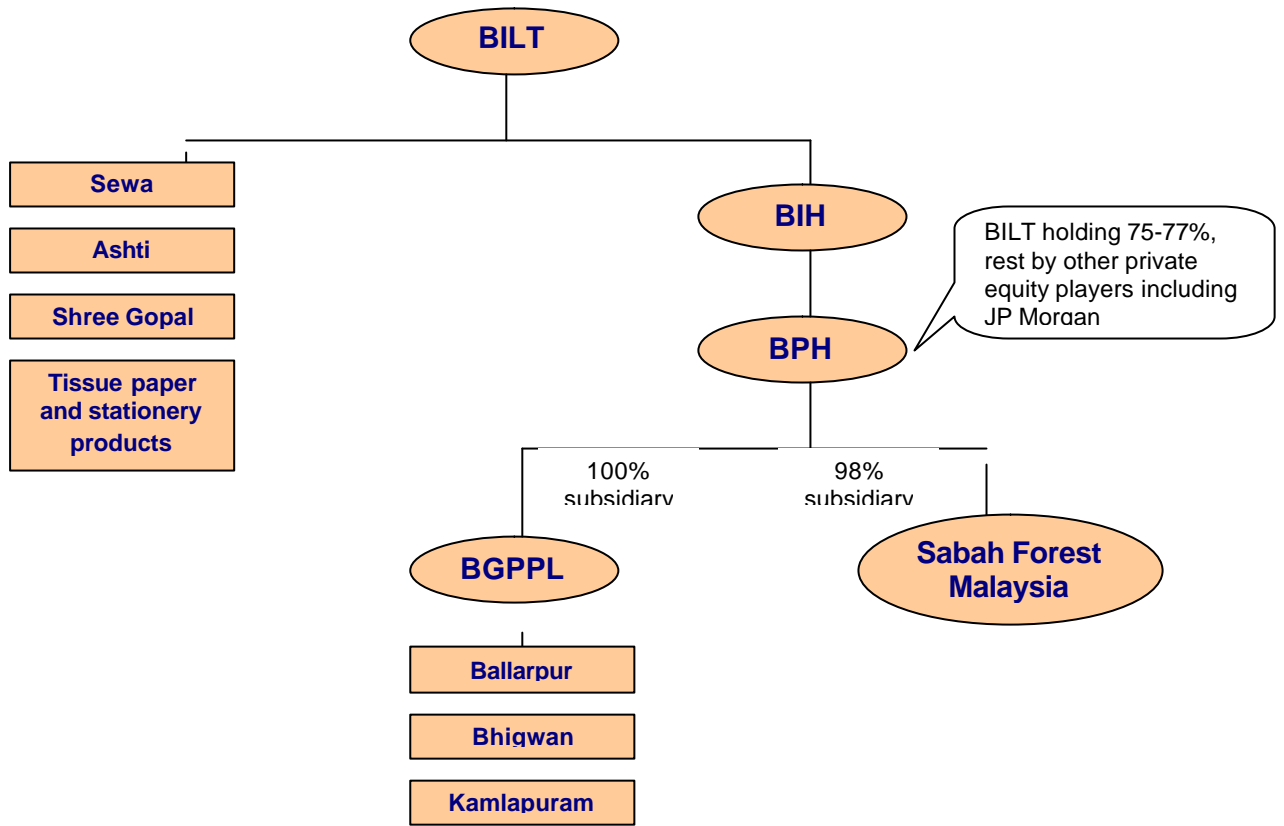
Post buyback BILT's equity share capital is likely to come down from Rs 1.85 bn to Rs 1.11 bn. This equity reduction will have positive impact on our earnings estimates and the same is likely to go up by approx 37% (on rough estimates). We have expected BILT to post an EPS of Rs 14.6 (excluding Sabah) in FY08 and possibly Sabah should contribute approx Rs 3 per share to FY 08 EPS. After equity reduction (before split), we expect consolidated EPS to go up to Rs 23.3 (rough estimates) in FY08.

BILT consolidated – Business structure pre reorganisation



Source- Company, Emkay share

BILT consolidated – Business structure post reorganisation



Source- Company, Emkay share

BILT – Plant Break - up

UNIT	Ballarpur	Shree Gopal	Bhigwan	Sewa	Kamlapuram	Ashti
Location	Maharashtra	Yamuna nagar, Haryana	Bhadalwadi, Maharashtra	Sewa, Orissa	Andhra Pradesh	Maharashtra
Paper Capacity (mt)	134,500	85,068	115,000	72,000	Nil	55,000
Pulp Capacity (mt)	130,000	52,200	Nil	43,000	98,550	Nil
Captive pulp requirement	114,325	72,308	74,750	61,200	-	46,750
Captive pulp surplus/ (deficit)	14%	-28%	-100%	-30%	-	-100%
Capacity Util	99%	91%	101%	93%	84%	-
CPP Capacity (MW)	27.5	24.3	30.0	13.4	15.0	0.0
CPP mode	Coal based	Coal based	Coal based	Coal based	Coal based	-
Coal Source	Western Colafields, Chandanpur	Eastern Coalfields	WCL, Nagpur	Mahanadi coalfields	Singareni Coaleries	-
Captive Chemical	Yes	No	No	No	No	No
Water Availability	Good	Good	Good	Good	Good	Good
Waste management	yes	yes	yes	yes	yes	yes
Other Technology		Blade coater with capacity of 30,000 mt	High speed paper machine	On line one sided coated paper of 36,000 mt		
Finished Products	Coated paper, copier and specialty paper	Coated, Uncoated, Specialty paper	High quality coated paper	Copier, coated paper, maplitho	Rayon grade pulp/ Paper Pulp	Copier, Maplitho and PWP
Raw material use	Bamboo, wood	Bamboo, wood	Imported pulp	Bamboo, wood	Bamboo, wood	Imported pulp
Raw material Source	Social farm forestry	Market Purchase	Imports	Market Purchase	Government and social farm forestry	Pulp from Ballarpur unit and imports
Transportation facility and reach	proximity to coal mines and forests	Proximity to north market	Proximity in sourcing imported pulp	Easy access to major highways, railway and airport	Easy availability of raw material	Proximity to markets

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