

May 25, 2010

ACCUMULATE

CMP	Target Price	
	Pre-Demerger	Post-Demerger
Rs2,453	Rs2,997	Rs 2,507
Sensex	16,501	

Price Performance

(%)	1M	3M	6M	12M
Absolute	(13)	(9)	6	12
Rel. to Sensex	(8)	(10)	9	(7)

Source: Bloomberg

Stock Details

Sector	Cement
Reuters	GRAS.BO
Bloomberg	GRASIM@IN
Equity Capital (Rs mn)	917
Face Value(Rs)	10
No of shares o/s (mn)	92
52 Week H/L	2,952/2,026
Market Cap (Rs bn/USD mn)	225/4,794
Daily Avg Volume (No of sh)	160119
Daily Avg Turnover (US\$mn)	9.4

Shareholding Pattern (%)

	Mar'10	Dec'09	Sep'09
Promoters	25.5	25.5	25.2
FII/NRI	37.9	37.2	37.2
Institutions	19.8	20.6	20.6
Private Corp	5.3	5.0	5.4
Public	11.5	11.7	11.7

Source: Capitaline

Under the proposal for restructuring its cement business (where Grasim will first hive off its cement assets into Samruddhi Cement Ltd (Samruddhi) and eventually merge it with that of Ultratech Cement (Ultratech)), Grasim stock is going ex-Samruddhi on 26th May 2010. We estimate Samruddhi's listing price (listing by June 2010) in the range of Rs500-550. Post de-merger of cement business, our SoTP based fair value for Grasim would come to ~Rs2507, which currently is ~Rs3000 (EV/ton of USD 120 for cement business and holding company discount of 20%, VSF business at 6X FY11 EV/EBIDTA). Based on CMP of ~Rs2400, we expect Grasim to trade at Rs1900 ex-Samruddhi. At CMP of Grasim, the implied holding co discount is close to 60%, highest seen by the stock since the announcement of swap ratio in mid November 2009. This huge discount, we believe is unjustified and expect the same to reduce going forward. Maintain our ACCUMULATE rating on Grasim & REDUCE rating on Ultratech.

Grasim to go ex- Samruddhi

Under the proposal for restructuring its cement business (where Grasim will first hive off its cement assets into Samruddhi Cement Ltd (Samruddhi) and eventually merge it with that of Ultratech Cement (Ultratech)), the board of directors of Grasim Industries (Grasim) have fixed 28th May 2010 as the record date for share entitlement of Samruddhi. We have highlighted here the chronology of the events for the merger.

Chronology & tentative timelines for the de-merger of Grasim's Cement business

De-merger Of Cement assets of Grasim Into Samruddhi	Already Over
Grasim Stock goes ex-Samruddhi	26th May 2010
Record date for share entitlement of Samruddhi	28th May 2010
Listing of Samruddhi Shares	June 2010
High Court application for merger of Samruddhi Into Ultratech	Underway
Completion of Samruddhi & Ultratech Merger	End July 2010

Under the swap ratio for the de-merger of cement business, each Grasim shareholders on 28th May 2010 will receive one share of Samruddhi. Eventually for merger of Samruddhi into Ultratech, the swap ratio has been finalized at 4:7, i.e. 4 shares of Ultratech, for every 7 shares held in Samruddhi. Ultratech's shareholding post merger would be, as shown in exhibit 1.

Financial Snapshot

	Net sales (Rs.mn)	EBIDTA (Rs.mn)	EBIDTA (%)	PAT (Rs.mn)	EPS (Rs.)	EPS growth (%)	ROCE (%)	PE (x)	EV/EBIDTA (x)	EV/Ton (USD)
FY09	184039	43298	23.5	21867	238.5	-24.3	22.3	11.9	4.8	125.3
FY010	199334	57867	29	30955	301	26.2	25.9	9.4	3.4	102.6
FY011E	205116	51984	25.3	25738	280.8	-13.8	19.9	10.1	3.4	95.3
FY012E	225685	53851	23.9	26684	320.2	14.0	19.1	8.9	2.4	74.6

*Note: Numbers not adjusted for De-merger of cement business

Exhibit 1: Ultratech's Shareholding pattern

Shareholding Pre Merger		Shares held (mn)	% Holding
Ultratech Current Equity	A	124.5	
Grasim	B	68.2	54.8%
Ultratech Minority Shareholders	C	56.3	45.2%
New Shares to be issued by Ultratech to Samruddhi (Based on Swap ratio of 4:7)	D	149.5	
To Grasim	E	97.2	65.0%
To Grasim Shareholders	F	52.3	35.0%
Shareholding Post Merger			
Grasim	B+E	165.4	60.33%
Grasim Shareholders	F	52.3	19.10%
Ultratech Minority Shareholders	C	56.3	20.57%
Total		274.0	

(Source: Company)

Exhibit 2: SCL's Shareholding pattern

Shareholders	Mn shares	% Holding
Grasim Industries	170	65
Grasim Shareholder	91.7	35
Total Equity	261.7	100

(Source: Company)

Samruddhi to list at Rs500-550

Since the swap ratio for the eventual merger of Ultratech and Samruddhi has been finalized at 4:7, the listing price of Samruddhi entirely depends upon the stock price movement of Ultratech. We estimate Samruddhi's listing price in the range of Rs500-550. Our estimate is based on two factors

- 1) Based on fair value of Ultratech post merger and
- 2) Based on intermediate price movement of Ultratech

(Source: Company)

Exhibit 3: Based on fair value of Ultratech post merger and

Equity value of consolidated cement business (See Exhibit 5)	At USD 120/ton	246552
Ultratech Equity (From Exhibit 1)	Mn shares	274.0
Ultratech fair Value	Rs/share	899.7
Ultratech Shares to be issued to Samruddhi	Mn shares	150
Value	Rsmn	134546
Samruddhi Equity (From Exhibit 2)	Mn Share	261.7
Samruddhi Fair value	Rs/share	514

(Source: Emkay Research)

Exhibit 4: Based on intermediate price movement of Ultratech

Ultratech Current Price (Rs/share)	1000	975	950	925	900
Ultratech Shares to be issued to Samruddhi (mn shares)	150	150	150	150	150
Value (Rs mn)	149543	145804	142066	138327	134589
Samruddhi's O/S equity (mn share)	261.7	261.7	261.7	261.7	261.7
Samruddhi's fair value (Rs/share)	571	557	543	529	514

(Source: Emkay Research)

Grasim SoTP fair value to come down to Rs2507 compared to Rs3000 currently

Post de-merger of cement business, our SoTP based fair value for Grasim would come to ~Rs2507, which currently is ~Rs3000. In our post demerger SoTP fair value we have valued the consolidated cement business (capacity of 48.8 mtpa) at an EV/ton of USD120 and assigned a holding company discount of 20% for Grasim holding in cement business. We have valued the VSF business at 6X FY11 EV/EBIDTA and Chemical business at 3X EV/EBIDTA.

Exhibit 5: Grasim SoTP fair value to come down to Rs2507 post de-merger

	Valuation measure	Rsmn	Rs/share	Pre-De-merger (Rs/share)	Post De-merger (Rs/share)
Enterprise Value of consolidated cement business'	Valued @ USD 120/ton	263250			
Net debt Of consolidated cement Business		16698			
Equity value of consolidated cement business		246552			
Grasim's Stake in cement business		60.3%			
Value of Grasim's stake in cement business		148745	1623	1623	1623
Holding Co disc			0%	20%	20%
Net Value		148744.6	1622.6	1298.1	1298.1
Value of Grasim Shareholders holding of 19.1% in Ultratech		47091	514	514	
Total value of cement business		195836	2136	1812	1298
ADD: Value of Non Cement Business					
Viscose Staple Fibre	6X EV/EBIDTA	74181	809	809	809
Chemical	3X EV/EBIDTA	3725	41	41	41
Other	3X EV/EBIDTA	2315	25	25	25
Total Value Of Non Cement Business		80221	875	875	875
Total value of Investments	@25% discount	40958	447	447	447
Total Enterprise value		317014	3458	3134	2620
Less:					
Standalone Debt		10380	113	113	113
Target Mcap		306634	3345	3020	2507

(Source: Emkay Research)

Current price implies, Grasim's ex-Samruddhi value at Rs1900

Based on CMP of ~Rs2400, we expect Grasim to trade at Rs1900 ex-Samruddhi. Our estimate is based on fair value of Rs514 for Samruddhi as shown in exhibit 5.

Exhibit 6: Sensitivity of holding company discount on SoTP (Pre-De-merger)

Rs/share					
Grasim's Stake in cement business (From Exhibit 5)	1623	1623	1623	1623	1623
Value of Grasim's stake in cement business	20%	30%	40%	50%	60%
Net Value	1298	1136	974	811	649
Grasim Shareholders Direct Holding in Ultratech - 19.1% (From exhibit 1)	514	514	514	514	514
Total value of cement business	1812	1650	1487	1325	1163
ADD: Value of Non Cement Business (From Exhibit 5)					
Viscose Staple Fibre	809	809	809	809	809
Chemical	41	41	41	41	41
Other	25	25	25	25	25
Total Value Of Non Cement Business	875	875	875	875	875
Total value of Investments (From Exhibit 5)	447	447	447	447	447
Total Enterprise value	3134	2971	2809	2647	2485
Less:					
Standalone Debt	113	113	113	113	113
Target Mcap	3020	2858	2696	2534	2371

(Source: Emkay Research)

Exhibit 7: Sensitivity of holding company discount on SoTP (Post -De-merger)

Rs/share					
Grasim's Stake in cement business (From Exhibit 5)	1623	1623	1623	1623	1623
Value of Grasim's stake in cement business	20%	30%	40%	50%	60%
Total value of cement business	1298	1136	974	811	649
ADD: Value of Non Cement Business (From Exhibit 5)					
Viscose Staple Fibre	809	809	809	809	809
Chemical	41	41	41	41	41
Other	25	25	25	25	25
Total Value Of Non Cement Business	875	875	875	875	875
Total value of Investments (From Exhibit 5)	447	447	447	447	447
Total Enterprise value	2620	2458	2295	2133	1971
Less:					
Standalone Debt	113	113	113	113	113
Target Mcap	2507	2344	2182	2020	1858

(Source: Emkay Research)

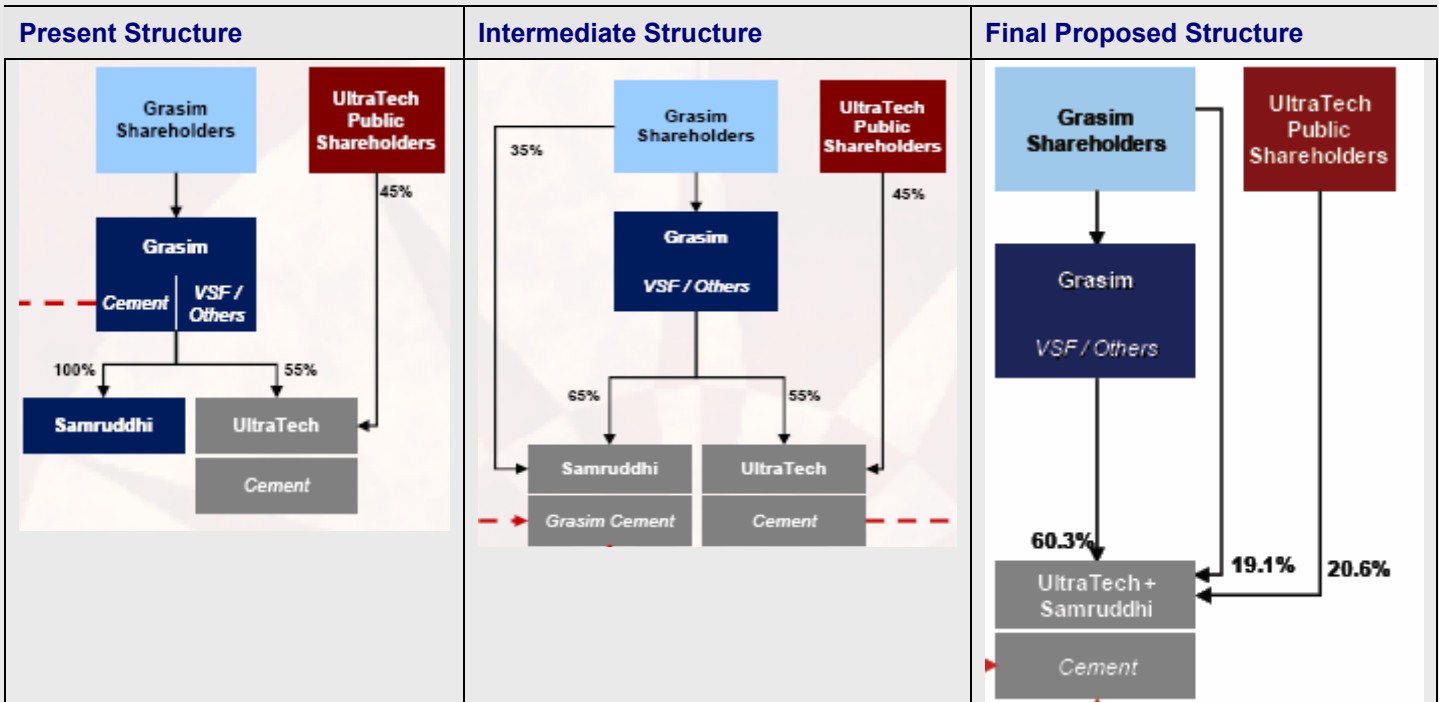
Current price implying ~60% holding company discount- Expect Holding co discount to go down - Maintain ACCUMULATE on Grasim- REDUCE on Ultratech

At current stock price of ~Rs2400 for Grasim, the implied holding co discount is 58%. The discount is the highest seen by the stock since the announcement of swap ratio in mid November 2009. This huge discount we believe is unjustified and expect the same to see correct going forward. Hence we maintain our ACCUMULATE rating on Grasim & REDUCE rating on Ultratech.

The restructuring proposal

Grasim to hive off cement ops to Samruddhi and merge it with Ultratech

Grasim Industries under the proposal of restructuring of its cement business is hiving off the cement assets into Samruddhi. Post the transfer of cement assets, Samruddhi will issue one equity share of face value Rs5 each to Grasim Shareholders for every one share held by them in Grasim. Upon the issue of shares, Grasim shareholders will directly hold 35% in SCL and 65% through Grasim (indirectly). Post the completion of scheme Samruddhi is proposed to be listed. To achieve the objective of consolidation of cement business under one entity, Samruddhi will be eventually merged with Ultratech and in consideration of merger of its cement business; Samruddhi will receive Ultratech shares in the ratio of 4:7.



Source: Company, Emkay Research

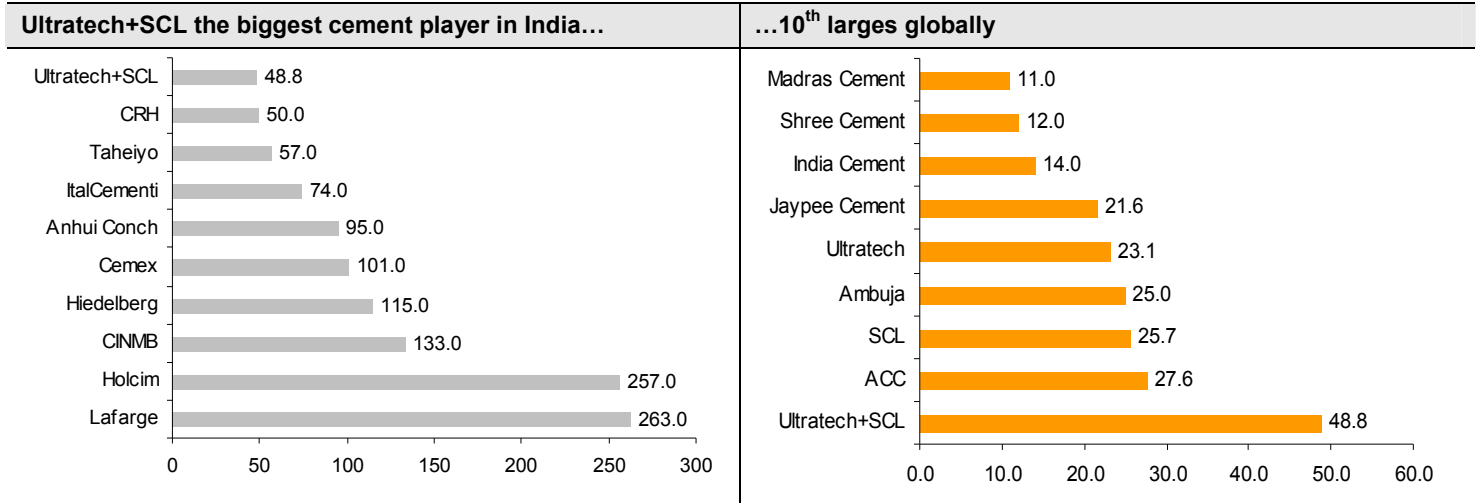
Ultratech's Shareholding pattern

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To Grasim	E	97.2	65.0%
To Grasim Shareholders	F	52.3	35.0%
Shareholding Post Merger			
Grasim	B+E	165.4	60.33%
Grasim Shareholders	F	52.3	19.10%
Ultratech Minority Shareholders	C	56.3	20.57%
Total		274.0	

(Source: Company)

Ultratech+SCL to be the biggest cement company in India – 10th largest globally

The merged entity will have a cement capacity of 48.8 mtpa by the end of FY2010, thereby creating India's single-largest cement entity by a big margin, ACC being the distant second with capacity 27.6 mtpa. The merger also makes Ultratech+SCL combine the tenth largest cement manufacturer in the world.



Source: Emkay Research, Company

Exhibit 8: Ultratech – SCL Combined Entity

Capacity		UltraTech	Samruddhi	Combined
Grey Cement	Million TPA	23.1	25.7	48.8
Composite Plants	No.	5	6	11
Grinding Units	No.	6	5	11
White Cement	Million TPA	-	0.6	0.6
Captive Thermal Power Plants	MW	236	268	504
RMC	No.	32 plants	36 plants	68 plants
	Million Cu. M	4.99	6.76	11.76
Key Investments - Subsidiaries		80% Equity in Lanka	100% Equity in Harish Cement Ltd.	Combined Investments
Market Share : Grey Cement		9%	10%	19%

Source: Company

Income Statement

Y/E, Mar (Rs. m)	FY08	FY09	FY10	FY11E	FY12E
Net Sales	170569	184039	199334	205116	225685
Growth (%)	20.9	7.9	8.3	2.9	10.0
Total Expenditure	121049	140741	141467	153132	171834
Growth (%)	19.3	16.3	0.5	8.2	12.2
Raw Materials Exp	37783	40813	37637	42108	46330
% of sales	22.2	22.2	18.9	20.5	20.5
Employee cost	8493	9536	10586	11644	12809
% of sales	5.0	5.2	5.3	5.7	5.7
Power & Fuel cost	29074	37557	35230	39055	42972
% of sales	17.0	20.4	17.7	19.0	19.0
Freight Charges	30163	23459	27503	27223	29953
% of sales	17.7	12.7	13.8	13.3	13.3
Admin & Other exp	2145	30283	30728	33102	39770
% of sales	1.3	16.5	15.4	16.1	17.6
EBIDTA	49520	43298	57867	51984	53851
Growth (%)	24.9	-12.6	33.6	-10.2	3.6
EBIDTA %	29.0	23.5	29.0	25.3	23.9
Other income	7446	4530	5356	5068	5518
Interest	2221	3104	3346	2776	2151
Depreciation	6625	8658	9947	11054	11698
EBT	48120	36066	49930	43221	45519
Tax	14658	9914	15705	13242	13972
Deferred Tax			0.0	0.0	0.0
EAT	33462	26152	34225	29979	31548
Growth (%)	41.8	-21.8	30.9	-12.4	5.2
EAT (%)	19.6	14.2	17.2	14.6	14.0
E/O items	2649.0	0.0	3360.7	0.0	0.0
Adjusted PAT	26248	21867	30955	25738	26684
EAT after min int	28897	21867	27595	25738	26684

Cash Flow

Cash Flow	FY08	FY09	FY10	FY11E	FY12E
Net Profit after Tax	33462	26152	34225	29979	31548
Add : Depreciation	6625	8658	9947	11054	11698
Add : Misc exp w/off					
Add : intangibles w/off					
changes in debtors	-1933	1947	-2087	-762	-985
changes in inventories	-3862	-4768	-1781	-1807	-2394
changes in creditors	8048	-1162	3818	2444	3383
changes in L & A	-4785	-353	0	0	0
Net changes in WC	-2532	-4336	-51	-125	4
Cash flow from Oper act	36972	34625	48560	40908	43249
Capital expenditure	-49243	-17921	-30432	-20930	-15630
Investments	6112	-19020	0	0	0
Cash Flow from Inv act	-42316	-36651	-30432	-20930	-15630
Borrowings	7040	3391	-4707	-7500	-10000
dividend paid	-2750	-2750	-4214	-3708	-3742
Issue of shares					
Cash Flow from fin act	4715	1715	-8921	-11208	-13742
changes in cash	-629	-310	9207	8770	13877
Opening balance	3692	2903	2270	11477	20247
Closing balance	2903	2270	11477	20247	34124

Balance Sheet

Y/E, Mar (Rs. m)	FY08	FY09	FY10P	FY11E	FY12E
Equity share capital	917	917	917	917	917
Preference share capital	-369	454	454	454	454
Share Application Money					
Reserves & surplus	91181	114209	140950	162980	185922
Networth	91729	115579	142320	164351	187292
Net Deferred tax liability	11575	15919	15919	15919	15919
Secured Loans	0	0	0	0	0
Unsecured Loans	0	0	0	0	0
Loan Funds	55771	59162	54455	46955	36955
Minority Interest	12694	16704	23845	28086	32950
Total Liabilities	171769	207364	236539	255311	273116
Gross Block	157198	210631	249435	268265	285205
Less: Depreciation	63397	68254	78201	89255	100953
Net block	93801	142377	171233	179010	184251
Capital work in progress	55335	19822	11450	13550	12240
Investment	16607	35627	35627	35627	35627
Current Assets	42802	45343	58418	69757	87014
Inventories	17443	22210	23991	25798	28192
Sundry debtors	10185	8239	10326	11088	12073
Cash & bank balance	2903	2270	11477	20247	34124
Loans & advances	12271	12625	12625	12625	12625
Other assets					
Current liabilities	36775	35806	40189	42633	46016
Current liabilities	30406	29245	33062	35506	38890
Provisions	6369	6562	7127	7127	7127
Net current assets	6027	9537	18229	27124	40998
Miscellaneous expenditure	0	1	0	0	0
Total Assets	171769	207364	236539	255311	273116

Key ratios

Valuations Ratios	FY08E	FY09	FY10	FY11E	FY12E
EPS	315.2	238.5	301.0	280.8	320.2
CEPS	387.5	333.0	409.5	401.3	460.6
Book Value Per Share	1004.3	1255.5	1547.2	1787.5	2241.6
Dividend Per Share	30.0	30.0	46.0	40.4	44.9
PER	9.0	11.9	9.4	10.1	8.9
P/CEPS	7.3	8.5	6.9	7.1	6.2
P/B (X)	2.8	2.3	1.8	1.6	1.3
EV/EBIDTA	4.1	4.8	3.4	3.4	2.4
EV/Sales	1.2	1.1	1.0	0.9	0.6
M-Cap/EBIDTA	5.2	6.0	4.5	5.0	4.4
M-Cap/sales	1.5	1.4	1.3	1.3	1.0
EV/Tonne (USD)	173.9	125.3	102.6	95.5	74.7
Financial ratios					
RoCE	35.6%	22.3%	25.9%	20.0%	19.2%
RoNW	31.4%	19.0%	19.5%	15.7%	14.3%
Net debt/ Equity (x)	0.58	0.49	0.30	0.16	0.02
Total Debt/Equity (x)	0.61	0.51	0.38	0.29	0.20
Dividend yield	1.06%	1.06%	1.62%	1.43%	1.58%

*Note: Numbers not adjusted for De-merger of cement business

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