Novonil Guha
91-22-**6632 2237**

Senior Research Analyst
NovonilGuha@PLIndia.com

Prabhudas Lilladher
Fulfilling investors' needs since 1944

Q4 FY07
Result Update

Grasim Industries

Market Performer | **Rs 2,442** | **April 26, 2007**

Strong topline growth overcome cost pressures

Company Details	
Market Cap:	Rs 223,879m
52-Week High/Low:	Rs 2,908/1,462
Bloomberg Code:	GRASIM@IN
Reuters Code:	GRAS.BO / NS
Shares O/s:	92m
Average Volume (3 months):	0.2m

Price Performance

(%)	1m	3m	12m
Absolute	17.9	(14.7)	2.7
Relative to the Sensex	9.5	(14.3)	(16.4)

Result Snapshot

Grasim's Q4 FY07 results matched our expectations, with recurring earnings, at Rs 4.37bn, up 69% yoy (our estimate, Rs 4.4bn). Sales rose 37% yoy to Rs 24.9bn (our estimate, Rs 22.8bn), mainly driven by higher-than-expected volumes in VSF and sponge iron. Robust realisations in VSF, cement and sponge iron helped overcome cost pressures (power, freight, pulp, naphtha and propane), resulting in a 544-bp expansion in the overall EBITDA margin, to 27.8%. While pulp prices are expected to be high, given the global supply tightness, we believe that strong VSF demand would aid in passing on cost pressures. However, with cement prices now under a freeze, the cement division is likely to post muted growth.

At a P/E of 10.8x FY08 consolidated earnings, valuations are inexpensive. However, with the lack of specific growth triggers in the cement division—constituting 52% (standalone) and 70% (consolidated) of sales—we feel the stock is fairly valued. We maintain an **MARKET PERFORMER** rating.

Quarterly Table *(Rs m)*

Y/e March	Q4 FY07	Q4 FY06	*YoY Gr. (%)*	Q3 FY07	FY06	FY07E	*YoY Gr. (%)*
Net Sales	**24,938**	**18,151**	***37.4***	**22,794**	**66,226**	**84,537**	***27.6***
Raw Materials	7,614	5,495	*38.6*	6,672	18,665	21,552	*15.5*
Staff Costs	1,121	1,038	*8.0*	1,113	4,067	4,596	*13.0*
Power & Fuel	3,397	2,872	*18.3*	3,114	10,597	11,673	*10.2*
Freight	2,873	2,172	*32.2*	2,611	7,442	9,893	*32.9*
Other Expenses	2,991	2,509	*19.2*	2,624	11,188	12,770	*14.1*
Total Expenditure	17,995	14,086	*27.8*	16,133	51,959	60,484	*16.4*
EBITDA	**6,942**	**4,065**	***70.8***	**6,661**	**14,267**	**24,052**	***68.6***
EBITDA Margin (%)	*27.8*	*22.4*	*544.2bp*	*29.2*	*21.5*	*28.5*	*690.9bp*
Depreciation	876	759	*15.3*	807	2,965	3,104	*4.7*
Other Income	776	575	*34.9*	444	1,563	1,809	*15.8*
EBIT	**6,843**	**3,881**	***76.3***	**6,298**	**12,865**	**22,757**	***76.9***
Interest	366	236	*55.5*	240	1,152	987	*(14.4)*
PBT	**6,476**	**3,645**	***77.7***	**6,058**	**11,713**	**21,771**	***85.9***
Extraordinary Income/(Expense)	371	41	*798.3*	-	495	-	-
PBT (After EO)	**6,847**	**3,687**	***85.7***	**6,058**	**12,208**	**21,771**	***78.3***
Tax	2,102	1,059	*98.5*	1,942	3,572	6,792	*90.1*
Tax Rate (%)	*30.7*	*28.7*		*32.1*	*29.3*	*31.2*	
Reported PAT	**4,745**	**2,627**	***80.6***	**4,116**	**8,635**	**14,978**	***73.5***
Adjusted PAT	**4,374**	**2,586**	***69.1***	**4,116**	**8,140**	**14,978**	***84.0***

(Stock price as on April 25, 2007)

Segment-wise break-up

Y/e March	Q4 FY07	Q4 FY06	*YoY Gr. (%)*	Q3 FY07
VSF				
Volume Sales *(t)*	68,588	60,636	*13.1*	67,061
Realisation *(Rs/t)*	95,002	82,575	*15.0*	96,479
EBITDA Margin (%)	*30.8*	*31.3*		*34.5*
Grey Cement				
Volume Sales *(m t)*	3.9	3.9	*1.3*	3.7
Realisation *(Rs/t)*	3,210	2,323	*38.2*	3,160
White Cement				
Volume Sales *(t)*	102,200	95,598	*6.9*	93,571
Realisation *(Rs/t)*	6,518	6,117	*6.6*	6,456
Cement EBITDA Margin (%)	*34.3*	*24.6*		*33.0*
Sponge Iron				
Volume Sales *(t)*	171,942	95,949	*79.2*	147,339
Realisation *(Rs/t)*	13,518	10,885	*24*	12,344
EBITDA Margin (%)	*15.5*	*(4.6)*		*12.8*

Result Highlights

Cement division (52% of sales)

Revenue from the cement division rose 40% yoy, fuelled by a 38% yoy improvement in average net realisations. However, volume growth, at 1.3% yoy, remained muted, constrained by installed capacity as the company has already been operating at 118% during the quarter. Higher cement prices helped overcome the rise in freight and fuel costs, significantly improving the EBITDA by 94% to Rs 4.7bn and expanding the EBITDA margin by 970bp to 34.3%.

VSF division (27% of sales)

Revenue in VSF was up 30.1% yoy, aided by both volumes and realisations. Higher VSF prices were fuelled partly by strong demand and by a rise in pulp prices, which grew 19% yoy. However qoq, prices declined by about 2% due to discounts and rebates along with a higher share of export volumes (which have lower realisations). Consequently, volume growth also rose by an impressive 13.1% yoy. Mounting pulp costs along with an increase in employee costs resulted in a 50-bp fall yoy in the EBITDA margin despite higher VSF prices.

Sponge Iron division (10% of sales)

Revenue from the sponge iron division rose an impressive 117%, chiefly due to the lower base. Sales volumes were up 79% yoy due to higher production and strong demand. While the restriction on gas supply continued, higher prices of sponge iron allowed the company to use more expensive substitutes (such as naphtha) to increase operating rates. Higher realisations (up 24% yoy) along with greater productivity helped better operating margins -- from -4.6% to 15.5%.

Valuations and Outlook

We expect VSF demand to remain robust from the shift of textile hubs to India, Pakistan and Bangladesh and a general preference for cellulose fibres. While pulp costs would remain a cause for concern, robust demand would allow the company to pass on the incremental costs to consumers. We expect VSF margins to be stable -- at 30-31% levels. However, the cement division is likely to see muted volume growth and flat realisations in FY08. Further, input cost for the cement division is expected to be absorbed by the company, given the absence of any price upside in FY08. We feel that the lack of triggers for cement would hamper the stock performance in the future. It currently trades at a PER of 10.8x FY08 estimates and at an EV/E of 6x. We maintain a **MARKET PERFORMER** rating.

Key Figures

Y/e March	FY05	FY06	FY07E	FY08E
Revenues *(Rs m)*	93,880	102,652	136,277	144,140
EBITDA *(Rs m)*	20,317	20,579	39,461	41,543
Margins (%)	*21.6*	*20.0*	*29.0*	*28.8*
PAT *(Rs m)*	10,081	9,311	19,571	20,765
EPS *(Rs)*	109.9	101.6	213.4	226.5
PER *(x)*	22.2	24.0	11.4	10.8
EV / E *(x)*	12.9	12.6	6.5	6.0
EV / Sales *(x)*	2.8	2.5	1.9	1.7
RoCE (%)	*21.3*	*17.4*	*32.8*	*30.5*
RoE (%)	*27.4*	*19.4*	*30.8*	*26.2*