

Grasim Industries Ltd

Weak VSF pricing show signs of stabilization

Grasim reported consolidated EBITDA of Rs10.3bn vs JPMe at Rs9.7bn and well ahead of the consensus estimates at Rs8.6bn. While UTCEM results were inline with expectations, standalone EBITDA came in at Rs3.4bn vs JPMe at Rs2.96bn and consensus at Rs2.6bn primarily driven by the better than expected VSF sales volume. Consol PAT in the quarter was Rs4.2bn below JPMe of Rs5.2bn due to lower other income and higher tax rate.

- Weak VSF prices showing signs of improvement:** VSF sales volume improved 44% q/q (last quarter volumes were impacted by production shutdown) and was better than expected (~79kt vs. JPMe 72kt). Average VSF realizations were inline with our expectation declining 18% q/q but management have highlighted that global VSF prices have shown marginal improvement in the 2Q. This should help recovery in realization in 3QFY12. Margin declined sharply with lower ASP to 28.5% (vs. 38.8% in 1QFY12). Demand in the near term is expected to be “*volatile due to macro economic conditions and Euro Zone uncertainties*”.
- Cement environment remains tough:** Management expects 2HFY12 demand growth of ~7-8% (which given the low base should not be difficult) and medium to long term growth of 8-9%. As per the company the current surplus scenario should subside gradually in next 2-3 years. The increasing energy costs (imported and domestic coal prices have increased sharply over the last year) have been highlighted as a cause of concern.
- Capex update:** Grasim reduced the cement capex guidance for FY12 from Rs51.4bn in the 1Q (which was reduced from Rs53.7bn guidance) to Rs47.1bn and has spent ~Rs11.3bn in the 1HFY12. The tough market condition and the delay in recovery of cement demand is likely slowing capex in projects, in our view.
- The company has scheduled a conference call on 24th October 2011 at 10AM IST.** Our earning estimates are currently under review.

Company description

Table 1: Grasim—P&L sensitivity metrics

Grasim Industries Ltd (Reuters: GRAS.BO, Bloomberg: GRASIM IN)

Rs in mn, year-end Mar	FY09A	FY10A	FY11E	FY12E	FY13E
Net Sales (Rs mn)	171,871	196,735	212,690	218,024	238,552
Net Profit (Rs mn)	21,853.2	27,351.4	22,647.9	21,797.4	23,770.0
EPS (Rs)	238.39	298.34	247.03	237.75	259.27
Net profit growth (%)	-10.7%	25.2%	-17.2%	-3.8%	9.0%
ROE	21.1%	22.7%	16.7%	14.7%	14.8%
P/E (x)	9.6	7.7	9.3	9.6	8.8
P/BV (x)	1.8	1.7	1.4	1.4	1.2

Source: Company data, Bloomberg, J.P. Morgan estimates.

Overweight

GRAS.BO, GRASIM IN

Price: Rs2,289.55

Price Target: Rs2,700.00

India

India Cement

Pinakin Parekh, CFA^{AC}

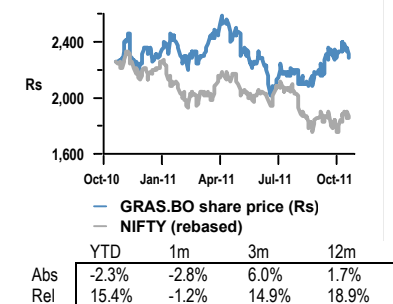
(91-22) 6157-3588
pinakin.m.parekh@jpmorgan.com

Neha Manpuria

(91-22) 6157-3589
neha.x.manpuria@jpmorgan.com

J.P. Morgan India Private Limited

Price Performance

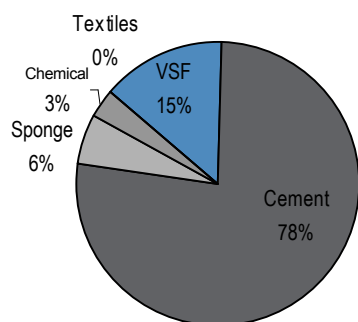


See page 6 for analyst certification and important disclosures, including non-US analyst disclosures.

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Grasim's principal activities include manufacture of viscose staple fibre (VSF), cement, sponge iron, chemicals and textiles. The company's VSF plants are located at Nagda in Madhya Pradesh, Kharach in Gujarat and Harihar in Karnataka, with an aggregate capacity of 333,975tpa. Grasim, along with its subsidiary UltraTech Cement Ltd., has a capacity of ~50MT and is a leading cement player in India.

Figure 1: Grasim—FY09 revenue break-up



Source: Company reports.

Table 2: EPS est—J.P. Morgan vs. consensus

Rs	J.P. Morgan	Consensus
FY12E	238	253
FY13E	259	268

Source: Bloomberg, J.P. Morgan estimates.

FY10E	EBITDA impact (%)	EPS impact (%)
Cement sales volume growth assumption		
Impact of each 1%	+/-2%	+/-2%
Cement average realization growth assumption		
Impact of each 1%	+/-2%	+/-2%
VSF sales assumption		
Impact of each 5%	+/-1%	+/-1%

Source: J.P. Morgan estimates.

Price target and valuation analysis

Our PT of Rs2700 is based on sum of the parts. We value VSF business at a multiple of 5.5x and our cement valuations are based on 20% holding company discount to our target valuations of UTCEM (we value UTCEM on \$130/MT).

The key risk remains the lack of visibility regarding the usage of VSF cash flows (steady state EBITDA of ~Rs13bn), which historically were invested in the cement business.

Table 3: Grasim Consolidated Quarterly Summary

Rs Mn, %	2QFY11	1QFY12	2QFY12	%y/y	%q/q
Net Sales	45,034	59,365	57,741	28%	-3%
EBITDA	7,856	16,399	10,278	31%	-37%
Interest	974	942	894	-8%	-5%
Depreciation	2,727	2,815	2,837	4%	1%
Other Income	980	1,085	1,068	9%	-2%
Profit before tax	5,134	13,728	7,615	48%	-45%
Less Current Tax	1,508	3,726	2,374		
Less Minority Share	393	2,485	1,062		
Recurring Profit	3,234	7,517	4,179	29%	-44%
EBITDA Margin (%)	17.4	27.6	17.8		
Tax rate (%)	29.4	27.1	31.2		

Source: Company reports, J P Morgan estimates.

Table 4: Grasim Standalone Quarterly Summary

Rs Mn, %	2QFY11	1QFY12	2QFY12	%y/y	%q/q
Net Sales	9,625	10,439	12,485	30%	20%
EBITDA	2,937	3,735	3,355	14%	-10%
Interest	103	106	107	4%	1%
Depreciation	453	351	356	-21%	2%
Other Income	1,324	804	1,707	29%	112%
Profit before tax	3,705	4,082	4,599	24%	13%
Less Current Tax	908	941	1,150	27%	22%
Recurring Profit	2,796	3,141	3,449	23%	10%
EBITDA Margin (%)	30.5	35.8	26.9		
Tax rate (%)	24.5	23.0	25.0		

Source: Company reports, J P Morgan estimates.

Valuations and Key Risks

We remain OW with a Mar-12 PT of Rs2700 based on sum of the parts. We value VSF business at a multiple of 5.5x and our cement valuations are based on 20% holding company discount to our target valuations of UTCCEM (we value UTCCEM on \$130/MT). The key risk remains the lack of visibility regarding the usage of VSF cash flows (steady state EBITDA of ~Rs13bn), which historically were invested in the cement business.

Table 5: GRASIM- SOTP Break Up

Rs bn, Rs	Mcap Contribution (Rs bn)
VSF 5.5x of FY12E EBITDA	72
Chemical 0.5x of FY12E Sales	3
Grasim standalone EV	74
Net debt - Standalone	-21
Grasim - Standalone M cap	95
20% Holding co discount on UTCCEM value	151
Total Grasim Implied M cap	246
Per share value (Rs/share)	2,700

Source: Company reports and J.P. Morgan estimates.

Grasim Industries Ltd: Summary of Financials

Income Statement					Cash flow statement				
Rs in millions, year end Mar	FY10	FY11E	FY12E	FY13E	Rs in millions, year end Mar	FY10	FY11E	FY12E	FY13E
Revenues	196,735	212,690	218,024	238,552	Net Income (Pre exceptionals)	27,351.4	22,647.9	21,797.4	23,770.0
% change Y/Y	14.5%	8.1%	2.5%	9.4%	Depr. & amortization	5,560	4,249	6,372	6,309
EBITDA	59,141	46,832	49,878	54,343	Change in working capital	3,271	-8,311	-1,434	-2,343
% change Y/Y	40.7%	-20.8%	6.5%	9.0%	Cash flow from operations	47,236	32,024	39,965	42,999
EBITDA Margin	30.1%	22.0%	22.9%	22.8%	Net Capex	-12,861	-23,711	-12,822	-41,500
EBIT	53,581	42,584	43,506	48,034	Free cash flow	34,375	8,314	27,143	1,499
% change Y/Y	38.2%	NM	2.2%	10.4%	Equity raised/(repaid)	-21,806	-6,522	-21,316	-11,050
EBIT Margin	27.2%	20.0%	20.0%	20.1%	Debt raised/(repaid)	-3,169	11,835	-22,327	0
Net Interest	-3,250	-4,056	-3,785	-3,785	Other	24,923	1,364	23,555	9,038
Earnings before tax	50,332	38,528	39,721	44,249	Dividends paid	-3,090	-2,090	-2,090	-2,090
% change Y/Y	39.5%	-23.5%	3.1%	11.4%	Beginning cash	2,270	2,370	2,844	28,873
Tax	15,890	9,576	10,794	12,016	Ending cash	2,370	2,844	28,873	26,269
as % of EBT	31.6%	24.9%	27.2%	27.2%	DPS	30.00	20.00	20.00	20.00
Net Income (Pre exceptionals)	27,351.4	22,647.9	21,797.4	23,770.0					
Minority interest	-7,090	-6,304	-7,130	-8,463					
PAT (Post minority interest)	27,351	22,648	21,797	23,770					
EPS-consolidated	298.34	247.03	237.75	259.27					
% change Y/Y	25.2%	(17.2%)	(3.8%)	9.0%					
Balance sheet					Ratio Analysis				
Rs in millions, year end Mar	FY10	FY11E	FY12E	FY13E	Rs in millions, year end Mar	FY10	FY11E	FY12E	FY13E
Inventories	21,835	27,229	24,792	27,222	EBITDA margin	30.1%	22.0%	22.9%	22.8%
Debtors	8,803	14,346	9,516	10,251	Operating margin	27.2%	20.0%	20.0%	20.1%
Cash and cash equivalents	2,370	2,844	28,873	26,269	Net margin	13.9%	10.7%	10.0%	10.0%
Loans and advances	12,371	14,378	15,000	15,000	Sales growth	14.5%	8.1%	2.5%	9.4%
Total CA	45,379	58,797	78,180	78,741	EPS growth	25.2%	(17.2%)	(3.8%)	9.0%
LT investments	66,759	79,185	58,120	58,120	Interest coverage (x)	18.20	11.55	13.18	14.36
Net fixed assets	212,286	237,039	216,324	244,715	Net debt to total capital	5.8%	-7.6%	8.1%	9.3%
Goodwill	20,071	24,191	16,824	16,824	Net debt to equity	8.3%	-10.3%	11.0%	11.3%
Total Assets	277,735	320,026	311,328	340,280	Sales/assets	0.76	0.71	0.69	0.73
Liabilities					Assets/equity	1.72	1.55	2.06	2.00
Provisions	-	-	-	-	ROE	22.7%	16.7%	14.7%	14.8%
Other current liabilities	8,522	7,771	9,644	10,466	ROCE	30.1%	21.6%	21.2%	23.3%
Total current liabilities	38,891	43,524	35,444	36,266					
Total debt	55,992	67,827	45,500	45,500					
Other liabilities	20,057	19,616	19,599	19,599					
Total Liabilities	114,941	130,967	100,543	101,365					
Shareholders' equity	125,246	145,586	151,107	170,199					

Source: Company reports and J.P. Morgan estimates.

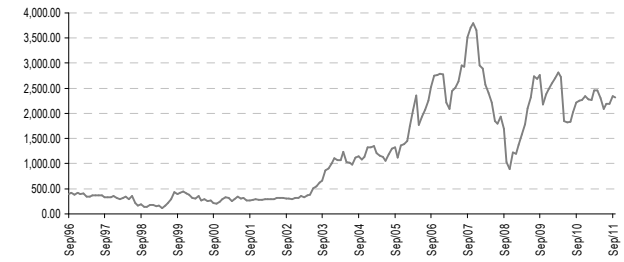
JPM Q-Profile
Grasim Industries Ltd. (INDIA / Materials)

As Of: 21-Oct-2011

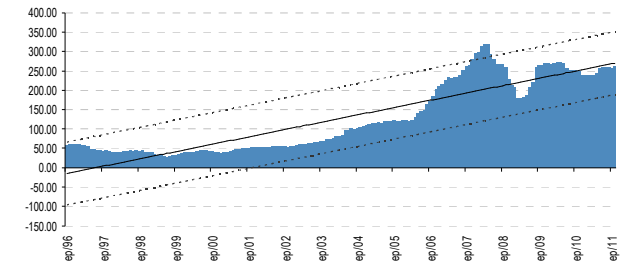
Global Equity Quantitative Analysis

Quant_Strategy@jpmorgan.com

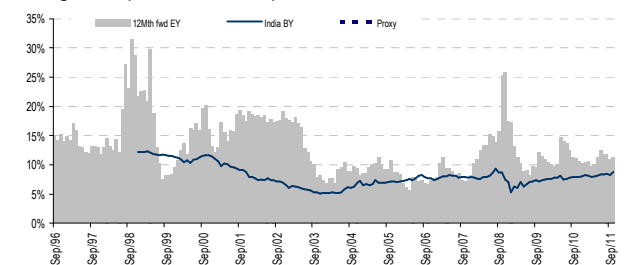
Local Share Price Current: **2315.25**



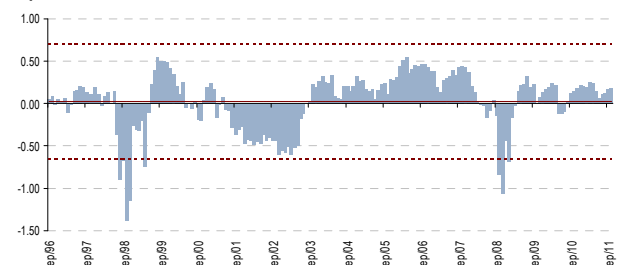
12 Mth Forward EPS Current: **260.44**



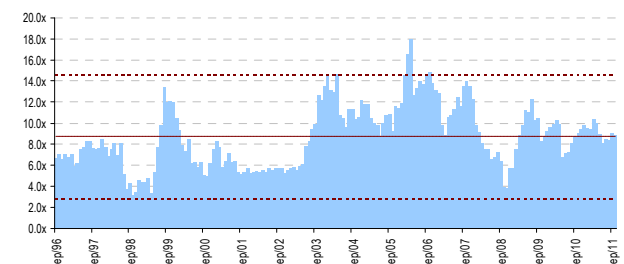
Earnings Yield (& local bond Yield) Current: **11%**



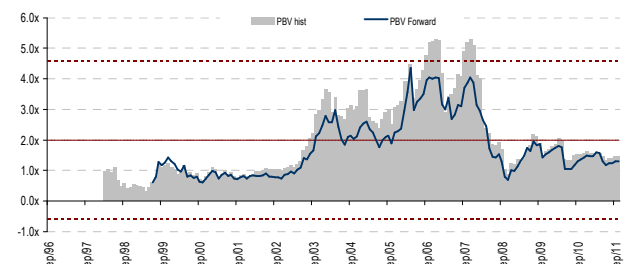
Implied Value Of Growth* Current: **18.52%**



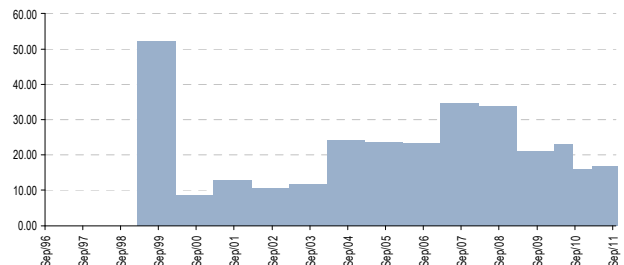
PE (1Yr Forward) Current: **8.9x**



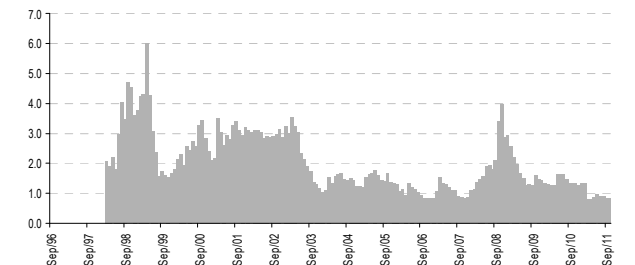
Price/Book Value Current: **1.5x**



ROE (Trailing) Current: **16.82**



Dividend Yield (Trailing) Current: **0.85**



Summary

Grasim Industries Ltd.		SEDOL		6099927		As Of:		21-Oct-11			
INDIA						Local Price:		2,315.25			
Materials						EPS:		260.44			
	Latest	Min	Max	Median	Average	2 S.D.+	2 S.D. -	% to Min	% to Max	% to Med	% to Avg
12mth Forward PE	8.89x	3.18	17.99	8.33	8.73	14.65	2.81	-64%	102%	-6%	-2%
P/BV (Trailing)	1.46x	0.31	5.30	1.53	2.00	4.58	-0.59	-79%	263%	5%	37%
Dividend Yield (Trailing)	0.85	0.81	6.02	1.64	2.01	3.99	0.04	-5%	605%	92%	136%
ROE (Trailing)	16.82	8.58	52.23	22.92	22.63	46.25	-0.98	-49%	211%	36%	35%
Implied Value of Growth	18.5%	-1.39	0.56	0.12	0.03	0.71	-0.66	-850%	201%	-34%	-85%

Source: Bloomberg, Reuters Global Fundamentals, IBES CONSENSUS, J.P. Morgan Calcs

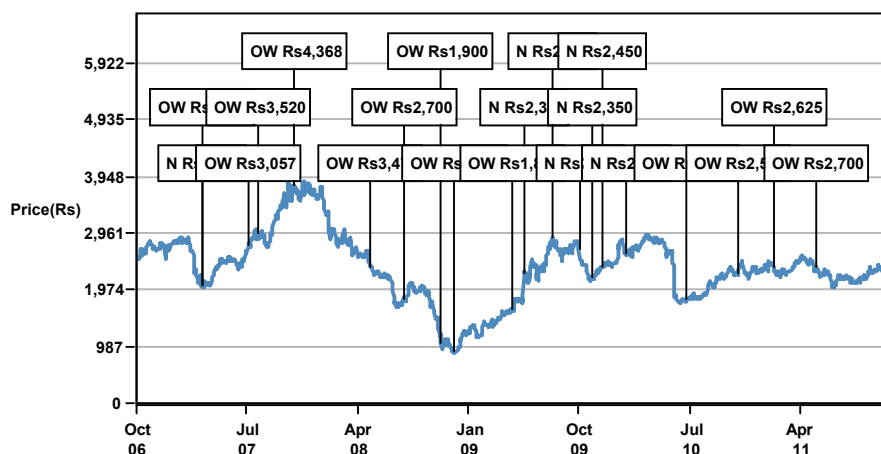
* Implied Value Of Growth = (1 - EY/Cost of equity) where cost of equity = Bond Yield + 5.0% (ERP)

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Grasim Industries Ltd (GRAS.BO) Price Chart



Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends. Initiated coverage Mar 13, 2007.

Date	Rating	Share Price (Rs)	Price Target (Rs)
13-Mar-07	N	2053.90	2800.00
14-Mar-07	OW	2053.90	2800.00
04-Jul-07	OW	2739.30	3057.00
30-Jul-07	OW	2945.35	3520.00
28-Oct-07	OW	3805.70	4368.00
04-May-08	OW	2380.45	3470.00
27-Jul-08	OW	1816.15	2700.00
24-Oct-08	OW	1033.70	1900.00
25-Nov-08	OW	898.90	1350.00
16-Apr-09	OW	1621.05	1850.00
20-May-09	N	2253.35	2300.00
28-Jul-09	N	2884.70	2550.00
05-Oct-09	N	2691.65	2300.00
01-Nov-09	N	2178.75	2350.00
26-Nov-09	N	2366.15	2450.00
23-Jan-10	N	2623.15	2640.00
25-Jun-10	OW	1798.75	2250.00
28-Oct-10	OW	2278.90	2550.00
26-Jan-11	OW	2367.95	2625.00
12-May-11	OW	2360.80	2700.00

The chart(s) show J.P. Morgan's continuing coverage of the stocks; the current analysts may or may not have covered it over the entire period.

J.P. Morgan ratings: OW = Overweight, N= Neutral, UW = Underweight

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	Overweight (buy)	Neutral (hold)	Underweight (sell)
J.P. Morgan Global Equity Research Coverage	47%	42%	11%
IB clients*	51%	44%	33%
JPMS Equity Research Coverage	45%	47%	7%
IB clients*	70%	60%	52%

*Percentage of investment banking clients in each rating category.

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