

Upgraded price target and recommendation

October 22, 2010

Reco	Previous Reco
Buy	Accumulate
CMP	Target Price
Rs 370	Rs 530
EPS change FY11E/12E (%)	60 / 44
Target Price change (%)	43
Nifty	6,102
Sensex	20,261

Price Performance

(%)	1M	3M	6M	12M
Absolute	21	27	44	91
Rel. to Nifty	20	12	24	59

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Agri-input & Chemicals
Bloomberg	GSFC@IN
Equity Capital (Rs mn)	798
Face Value(Rs)	10
No of shares o/s (mn)	80
52 Week H/L	385/160
Market Cap (Rs bn/USD mn)	29/654
Daily Avg Volume (No of sh)	201788
Daily Avg Turnover (US\$m)	1.4

Shareholding Pattern (%)

	S'10	J'10	M'10
Promoters	37.8	37.8	37.8
FII/NRI	6.9	6.5	7.0
Institutions	28.2	27.9	25.1
Private Corp	10.8	10.6	11.4
Public	16.3	17.1	18.7

Source: Capitaline

Rohan Gupta

rohan.gupta@emkayglobal.com
+91 22 6612 1248

Pragya Bhardwaj

pragya.bhardwaj@emkayglobal.com
+91 22 6612 1272

- **Q2FY11 PAT growth of 168% to Rs 2.1 bn was ahead of estimates driven by strong results of fertiliser and chemicals**
- **Fertilisers EBIT tripled to Rs 1.8 bn on the back of NBS policy while chemicals EBIT doubled to Rs 1.3 bn due to favourable spread in caprolactum**
- **Upgrade FY11E/FY12E EPS by 60%/44%, price target by 43% to Rs 530 and recommendation from ACCUMULATE to BUY**
- **At our target price, stock trades at FY12E P/BV of 1.4x and EV/EBITDA of 3.8x - a discount of ~50% to other players**

Strong margins in both the segments drove PAT by 168%

GSFC's Q2FY11 results positively surprised us with PAT growth of 168% to Rs 2.1 bn, ahead of our estimates of Rs 1.1 bn. Both the segments posted strong results with EBIT margins of 19.8% in fertilisers and 32.6% in chemicals against our expectations of 10% and 26%, respectively. With higher margins in both the segments, aggregate EBITDA margins improved by 960 bps yoy to 24.4% and EBITDA increased by 126% yoy to Rs 3.2 bn. Revenue growth of 37% to Rs 13 bn against our expectations of Rs 10 bn also contributed to the quantum jump in PAT.

Increase in fertiliser contribution to EBIT from 46% to 56% should result in stable earnings

We believe that with the improved profitability of the fertiliser segment, EBIT contribution from fertilisers is likely to increase from 46% in FY10 to 56% by FY12E. We argue that the fertiliser segment margins are more stable (post the introduction of NBS scheme) than chemicals segment due to price volatility and commodity nature of the chemicals business. We also argue that the fertiliser business with strong growth visibility and stable margins should command higher valuations than chemicals and rising contribution of fertiliser segment should trigger re-rating of the stock in near future.

Upgraded earnings, price target and recommendation to BUY

Sharp jump in fertiliser segment margins post NBS scheme, favourable spread in GSFC's chemicals business and strong H1FY11 results have triggered FY11E EPS upgrades by 60% to Rs 70.4. We also upgrade FY12E EPS by 44% to Rs 66.3.

GSFC's valuations continue to remain compelling at FY11E P/E of 5.3x, EV/EBITDA of 2.5x and P/BV of 1.1x. With strong investment book of Rs 9.5 bn (per share Rs 118), though strategic in nature, we find the stock extremely attractive and upgrade our price target by 43% from Rs 370 to Rs 530 based on 8x FY12 EPS (in line with historical average). However with improved visibility and rising contribution of fertiliser division, we expect stock to re-rate in medium term with further upside on our price target. At our target price, the stock trades at 1.4x FY12E book value and EV/EBITDA of 3.8x which is at significant discount of ~50% to other complex fertiliser companies. Subsequently we change our recommendation from ACCUMULATE to BUY. Inaccessible management and volatile earnings in chemical segment are key risks to our recommendation.

Financial Snapshot

Rs Mn

YE-Mar	Net	EBITDA		EPS		RoE		EV/	
	Sales	(Core)	(%)	PAT	(Rs)	% chg	(%)	P/E	EBITDA P/BV
FY09	58,808	8,509	14.5	4,994	62.7	114.2	29.3	5.9	3.1 1.5
FY10	40,192	4,477	11.1	2,545	31.9	(49.0)	12.5	11.6	7.0 1.4
FY11E	46,034	9,188	20.0	5,611	70.4	120.5	23.5	5.3	2.5 1.1
FY12E	49,220	8,928	18.1	5,285	66.3	(5.8)	18.4	5.6	2.3 1.0

Key Financials – Quarterly

Rs mn

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)	YTD'11	YTD'10	YoY (%)
Revenue	9,522	11,413	7,825	10,668	13,007	36.6	21.9	23,674	20,953	13.0
Expenditure	8116	9513	6261	8831	9834	21.2	11.4	18666	19022	(1.9)
<i>as % of sales</i>	<i>85.2</i>	<i>83.3</i>	<i>80.0</i>	<i>82.8</i>	<i>75.6</i>			<i>78.8</i>	<i>90.8</i>	
Consumption of RM	5,616	6,855	4,530	6,223	7,366	31.2	18.4	13,589	14,037	(3.2)
<i>as % of sales</i>	<i>59.0</i>	<i>60.1</i>	<i>57.9</i>	<i>58.3</i>	<i>56.6</i>			<i>57.4</i>	<i>67.0</i>	
Power & Fuel	765	785	678	818	792	3.4	(3.2)	1,609	1,555	3.5
<i>as % of sales</i>	<i>8.0</i>	<i>6.9</i>	<i>8.7</i>	<i>7.7</i>	<i>6.1</i>			<i>6.8</i>	<i>7.4</i>	
Employee Cost	627	785	853	625	772	23.1	23.6	1,397	1,265	10.5
<i>as % of sales</i>	<i>6.6</i>	<i>6.9</i>	<i>10.9</i>	<i>5.9</i>	<i>5.9</i>			<i>5.9</i>	<i>6.0</i>	
Other expenditure	1,107	1,087	200	1,165	905	(18.3)	(22.4)	2,070	2,165	(4.4)
<i>as % of sales</i>	<i>11.6</i>	<i>9.5</i>	<i>2.6</i>	<i>10.9</i>	<i>7.0</i>			<i>8.7</i>	<i>10.3</i>	
EBITDA	1,407	1,901	1,564	1,836	3,172	125.5	72.8	5,009	1,931	159.4
Depreciation	356	356	352	343	358	0.6	4.3	701	702	(0.0)
EBIT	1,051	1,545	1,212	1,493	2,814	167.8	88.5	4,307	1,229	250.3
Other Income	212	256	365	146	438	107.0	200.2	584	509	14.8
Interest	85	71	56	41	41	(52.5)	-	81	180	(54.8)
PBT	1,177	1,731	1,521	1,598	3,212	172.8	101.0	4,810	1,559	208.6
Total Tax	406	592	233	512	1,142	181.5	122.9	1,654	521	217.2
Adjusted PAT	772	1,139	1,288	1,086	2,070	168.3	90.6	3,156	1,037	204.3
(Profit)/loss from JV's/Ass/MI	-	-	-	-	-			-	-	
APAT after MI	772	1,139	1,288	1,086	2,070	168.3	90.6	3,156	1,037	204.3
Extra ordinary items	0	0	-920	0	0			0	0	
Reported PAT	772	1,139	368	1,086	2,070	168.3	90.6	3,156	1,037	204.3
Reported EPS	9.7	14.3	4.6	13.6	26.0	168.3	90.6	39.6	13.0	204.3

Margins (%)						(bps)	(bps)			(bps)
EBIDTA	14.8	16.7	20.0	17.2	24.4	962	718	21.2	9.2	1,194
EBIT	11.0	13.5	15.5	14.0	21.6	1,060	764	18.2	5.9	1,233
EBT	10.1	12.9	14.8	13.6	21.3	1,118	771	17.9	5.0	1,284
PAT	8.1	10.0	16.5	10.2	15.9	781	574	13.3	5.0	838
Effective Tax rate	34.5	34.2	15.3	32.0	35.6	109	350	34.4	33.5	93

Source: Company, Emkay Research

Revision Table

Rs mn	FY11E			FY12E		
	Old Estimates	New Estimates	% Change	Old Estimates	New Estimates	% Change
Net sales	40867	46034	12.6%	41487	49220	18.6%
EBITDA	6173	9188	48.8%	6507	8928	37.2%
EBITDA %	15.1%	20.0%	485	15.7%	18.1%	245
PAT	3502	5611	60.2%	3663	5285	44.3%
EPS	43.9	70.4	60.4%	46.0	66.3	44.2%

Fertiliser segment benefited from NBS scheme

Fertiliser segment EBIT increased by 198% to Rs 1.8 bn (ahead of estimates Rs 735 mn). Complex fertilisers industry has benefited from the recently introduced (Apr '10) Nutrient Based Subsidy (NBS) scheme which has helped efficient players in improving their margins. GSFC enjoys benefits of captive ammonia plant as a result of which its EBIT margins in fertiliser segment improved from 6.7% in FY10 to 16.8% in H1FY11. During the quarter fertiliser revenues increased by 39% yoy to Rs 9.1 bn. Urea fertiliser sales volumes for GSFC declined by 22% (to 60 thousand mt) while complex fertiliser sales increased by 16% (to 349 thousand mt).

EBIT margins in fertiliser segment improved from 6.7% in FY10 to 16.8% in H1FY11.

Chemicals segment posted higher margins on increased realisations

Chemicals EBIT increased sharply by 95% yoy to Rs 1.3 bn against expected Rs 847 mn. During the quarter, we expect that company's caprolactum business (contributes ~50% to chemical revenues) has benefited from higher prices resulting into improved spread and margins. Chemicals segment revenues also increased by 31% yoy to Rs 3.9 bn.

Caprolactum business has benefited from higher prices resulting into improved spread

Segmental results Rs mn

Y/E Mar	Q2FY10	Q1FY11	Q2FY11	% YoY	% QoQ
Revenues					
Fertilisers	6560	7853	9133	39.2	16.3
Chemicals	2962	2814	3873	30.8	37.6
Total	9522	10668	13007	36.6	21.9
Earnings					
Fertilisers	606	1049	1808	198.2	72.4
Chemicals	648	610	1264	95.2	107.1
Total	1254	1659	3072	145.0	85.2
Segment margins (%)				(chng bps)	(chng bps)
Fertilisers	9.2	13.4	19.8	1055	644
Chemicals	21.9	21.7	32.6	1077	1094
Total	13.2	15.6	23.6	1045	807

Source: Company, Emkay Research

Key Financials

Income Statement

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Net Sales	58,808	40,192	46,034	49,220
Growth (%)	65.4	(31.7)	14.5	6.9
Expenditure	50,299	35,715	36,845	40,292
Materials Consumed	38,193	25,422	28,403	30,565
Power & Fuel	3,069	3,019	3,222	3,199
Employee Cost	3,890	2,902	3,222	3,445
Other Exp	5,148	4,372	1,998	3,082
EBITDA	8,509	4,477	9,188	8,928
Growth (%)	79.4	(47.4)	105.3	(2.8)
EBITDA margin (%)	14.5	11.1	20.0	18.1
Depreciation	1,430	1,409	1,417	1,600
EBIT	7,078	3,067	7,771	7,328
EBIT margin (%)	12.0	7.6	16.9	14.9
Other Income	713	1,130	984	800
Interest expenses	392	306	281	240
PBT	7,400	3,891	8,474	7,888
Tax	2,406	1,346	2,863	2,603
Effective tax rate (%)	32.5	34.6	33.8	33.0
Adjusted PAT	4,994	2,545	5,611	5,285
Growth (%)	114.1	(49.0)	120.5	(5.8)
Net Margin (%)	8.5	6.3	12.2	10.7
(Profit)/loss from JVs/Ass/MI	-	-	-	-
Adjusted PAT After JVs/Ass/MI	4,994	2,545	5,611	5,285
E/O items	-	-	-	-
Reported PAT	4,994	2,545	5,611	5,285
PAT after MI	4,994	2,545	5,611	5,285
Growth (%)	114.1	(49.0)	120.5	(5.8)

Cash Flow

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
PBT (Ex-Other income)	6,687	2,761	7,490	7,088
Depreciation	1,430	1,409	1,417	1,600
Interest Provided	392	306	281	240
Other Non-Cash items	688	(692)	(294)	(95)
Chg in working cap	241	(6,658)	4,899	(783)
Tax paid	-2,406	-1,346	-2,863	-2,603
Operating Cashflow	7,032	-4,220	10,930	5,446
Capital expenditure	(1,230)	(1,472)	(3,000)	(3,000)
Free Cash Flow	5,802	-5,692	7,930	2,446
Other income	713	1,130	984	800
Investments	(3,847)	1,811	-	-
Investing Cashflow	-3,134	2,941	984	800
Equity Capital Raised	-	-	-	-
Loans Taken / (Repaid)	(2,355)	3,636	-	-
Interest Paid	(392)	(306)	(281)	(240)
Dividend paid (incl tax)	(359)	(359)	(359)	(558)
Income from investments	0	0	0	0
Others	0	0	0	0
Financing Cashflow	-3,105	2,971	-640	-798
Net chg in cash	-438	220	8,275	2,449
Opening cash position	819	381	601	8,876
Closing cash position	381	601	8,876	11,325

Balance Sheet

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Equity share capital	797	797	797	797
Reserves & surplus	18,518	20,644	25,602	30,234
Net worth	19,315	21,441	26,399	31,031
Minority Interest	0	0	0	0
Secured Loans	1,548	1,748	1,748	1,748
Unsecured Loans	1,692	5,128	5,128	5,128
Loan Funds	3,240	6,876	6,876	6,876
Net deferred liabilities	1,716	1,497	1,497	1,497
Total Liabilities	24,271	29,814	34,772	39,404
Gross Block	32,153	32,316	34,135	37,135
Less: Depreciation	20,130	21,501	22,919	24,519
Net block	12,023	10,815	11,216	12,616
Capital work in progress	509	1,819	3,000	3,000
Investments	6,061	4,250	4,250	4,250
Current Assets	14,631	21,037	27,762	31,518
Inventories	7,456	6,111	6,937	7,417
Sundry debtors	4,807	6,216	5,045	5,394
Cash & bank balance	381	601	8,876	11,325
Loans & advances	1,987	8,109	6,905	7,383
Other current assets	-	-	-	-
Current lia & Prov	8,954	8,107	11,457	11,980
Current liabilities	4,690	4,217	7,567	8,091
Provisions	4,264	3,889	3,889	3,889
Net current assets	5,677	12,930	16,306	19,538
Misc. exp	-	-	-	-
Total Assets	24,271	29,814	34,772	39,404

Key ratios

Y/E, Mar	FY09	FY10	FY11E	FY12E
Profitability (%)				
EBITDA Margin	14.5	11.1	20.0	18.1
Net Margin	8.5	6.3	12.2	10.7
ROCE	33.0	15.5	27.1	21.9
ROE	29.3	12.5	23.5	18.4
RoIC	38.1	15.2	37.2	37.1
Per Share Data (Rs)				
EPS	62.7	31.9	70.4	66.3
CEPS	80.6	49.6	88.2	86.4
BVPS	242.4	269.0	331.3	389.4
DPS	4.5	4.5	5.0	7.0
Valuations (x)				
PER	5.9	11.6	5.3	5.6
P/CEPS	4.6	7.5	4.2	4.3
P/BV	1.5	1.4	1.1	1.0
EV / Sales	0.4	0.8	0.5	0.4
EV / EBITDA	3.1	7.0	2.5	2.3
Dividend Yield (%)	1.2	1.2	1.9	1.9
Gearing Ratio (x)				
Net Debt/ Equity	-16.6	9.4	-23.7	-28.0
Net Debt/EBITDA	-0.4	0.5	-0.7	-1.0
Working Cap Cycle (days)	47.0	73.6	35.0	35.0

Recommendation History: Gujarat Sate Fertilisers – GSFC IN

Date	Reports	Reco	CMP	Target
03/08/2010	Gujarat Sate Fertilisers Q1FY11 Result Update	Accumulate	312	368
25/01/2010	Gujarat Sate Fertilisers Q3FY10 Result Update	Hold	214	254
03/11/2009	Gujarat Sate Fertilisers Q2FY10 Result Update	Hold	164	188
04/02/2009	Gujarat Sate Fertilisers Q3FY09 Result Update	Hold	86	107

Recent Research Reports

Date	Reports	Reco	CMP	Target
15/10/2010	Rallis India Q2FY11 Result Update	Buy	1,416	1,800
12/10/2010	Kajaria Ceramics Q2FY11 Result Update	Buy	80	91
03/08/2010	Tata Chemicals Q1FY11 Result Update	Accumulate	349	393
03/08/2010	GNFC Q1FY11 Result Update	Buy	115	157

Emkay Global Financial Services Ltd.

Paragon Center, H -13 -16, 1st Floor, Pandurang Budhkar Marg, Worli, Mumbai – 400 013. Tel No. 6612 1212. Fax: 6624 2410

DISCLAIMER: This document is not for public distribution and has been furnished to you solely for your information and may not be reproduced or redistributed to any other person. The manner of circulation and distribution of this document may be restricted by law or regulation in certain countries, including the United States. Persons into whose possession this document may come are required to inform themselves of, and to observe, such restrictions. This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. No person associated with Emkay Global Financial Services Ltd. is obligated to call or initiate contact with you for the purposes of elaborating or following up on the information contained in this document. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon. Neither Emkay Global Financial Services Ltd., nor any person connected with it, accepts any liability arising from the use of this document. The recipient of this material should rely on their own investigations and take their own professional advice. Opinions expressed are our current opinions as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. We and our affiliates, officers, directors, and employees world wide, including persons involved in the preparation or issuance of this material may; (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company (ies) discussed herein or may perform or seek to perform investment banking services for such company(ies) or act as advisor or lender / borrower to such company(ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. The same persons may have acted upon the information contained here. No part of this material may be duplicated in any form and/or redistributed without Emkay Global Financial Services Ltd.'s prior written consent. No part of this document may be distributed in Canada or used by private customers in the United Kingdom. In so far as this report includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.