Grasim Industries

Performance Highlights

Grasim Industries (Grasim) posted a robust 3QFY2010 consolidated performance on the Bottom-line front (up by 55.7% yoy), boosted by an outstanding performance by its VSF business. The VSF division posted its highest ever volumes of 81,300mt and also recorded an OPM of 41.8%, resulting in a 536% surge in operating profit to Rs403.7cr (Rs63.5cr). The cement business clocked a healthy 19% growth in operating profits, on account of higher volumes and lower energy prices. The company's net profit grew by 55.7% to Rs715.5cr (Rs459.6cr) during the quarter. After the results, we have revised our EPS estimates for FY2010E upward from Rs309 to Rs336. The stock trades at a P/E of 7.9x and at an EV/EBITDA of 4.5x, according to its FY2012E estimates. **We upgrade the stock to Accumulate from Neutral.**

Stellar performance in the VSF business drives Bottom-line growth: During 3QFY2010, the VSF business's Top-line grew by 71% to Rs962.4cr (Rs563.9cr), aided by a 51% growth in sales volumes and a 13% growth in realisation to Rs109,600 per tonne. The cement business's top-line grew by 7% to Rs3,635cr. Grasim reported a robust 44% growth in operating profit to Rs1,440cr, while its net profit grew by 55.7% to Rs715.5cr (Rs459.6cr).

Outlook and Valuation: The stock trades at a P/E of 7.9x and at an EV/EBITDA of 4.5x, according to its FY2012E estimates. We have valued the company's 60.3% stake in Ultratech (post demerger of Samruddhi) at an average of an EV/tonne of US $105/Tonne and an EV/EBITDA of 6.5x FY2012E, after providing 15% holding company discount to arrive at a value of Rs1,670/share. We have arrived at a value of Rs623/share for Grasim shareholder's direct holding in Ultratech (post demerger). We have valued the VSF business at 5x EV/EBITDA, implying a P/BV of 1.75x on an FY2012E basis. Hence, our SOTP Fair Value for Grasim works out to Rs2,861. We upgrade the stock to Accumulate from Neutral.

ACCUMULATE

CMP	Rs2,553
Target Price	Rs2,861
Investment Period	15 Months

Stock Info	
Sector	Cement
Market Cap (Rs cr)	23,406
Beta	0.7
52 WK High / Low	2,938/1,150
Avg. Daily Volume	50,150
Face Value (Rs)	10
BSE Sensex	16,290
Nifty	4,853
Reuters Code	GRAS.BO
Bloomberg Code	GRASIM@IN

Shareholding Pattern (%)	
Promoters	25.5
MF/Banks/Indian FIs	25.6
FII/NRIs/OCBs	37.2
Indian Public	11.7

Abs. (%)	3m	1yr	3yr
Sensex	(0.4)	80.9	14.1
Grasim	16.7	116.2	(10.8)

Key Financials (Consolidated)

Y/E March (Rs cr)	FY2009	FY2010E	FY2011E	FY2012E
Net Sales	**18,404**	**19,544**	**19,340**	**21,096**
% chg	*8.4*	*6.2*	*(1.0)*	*9.1*
Adj. Net Profit	**2,187**	**3,079**	**2,411**	**2,979**
% chg	*(24.4)*	*40.8*	*(21.7)*	*23.6*
OPM (%)	23.5	30.0	24.9	27.0
EPS (Rs)	**238**	**336**	**263**	**325**
P/E (x)	10.9	7.6	9.7	7.9
P/BV (x)	2.1	1.6	1.4	1.2
RoE (%)	21.3	23.7	15.2	16.0
RoCE (%)	13.0	15.2	11.2	12.7
EV/Sales (x)	1.6	1.4	1.4	1.2
EV/EBITDA (x)	6.9	4.7	5.5	4.5

Source: Company, Angel Research

Rupesh Sankhe
Tel: 022 – 4040 3800 Ext: 319
E-mail: rupeshd.sankhe@angeltrade.com

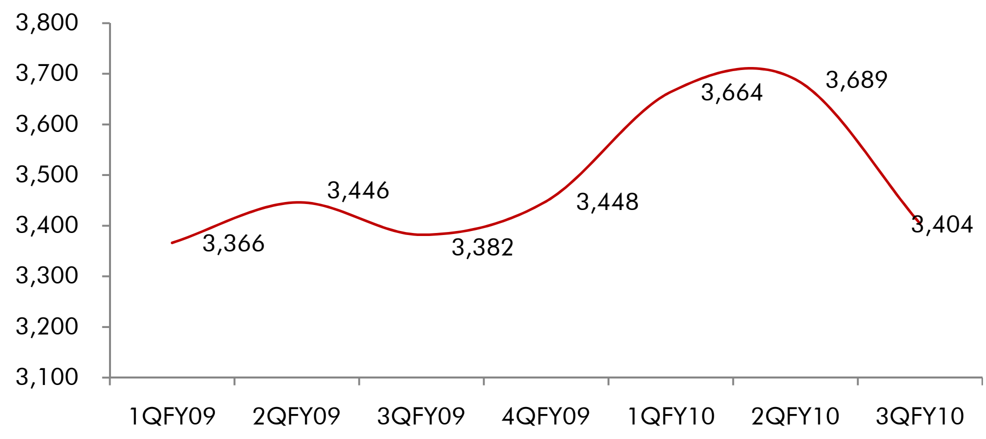
V Srinivasan
Tel: 022 – 4040 3800 Ext: 330
E-mail: v.srinivasan@angeltrade.com

Segmental Performance

Cement Business

3QFY2010 turned out to be a good quarter for the company's cement business. The revenues of the cement division were higher by 7% yoy (on a consolidated basis) at Rs3,635cr (Rs3,384cr). The consolidated cement sales volume was up by 14%, aided by a 29% and 19% growth in the offtake by the northern and eastern regions, respectively. However, the sales volume was up by a meager 9% in the southern region, due to the floods and the political unrest. The company's standalone cement sales volumes were also higher by 17% yoy to 4.8mn tonnes (4.1mn tonnes), aided by a 25% growth in installed capacity to 22.6mtpa. The company's standalone Cement realisations for the quarter were flat at Rs3,404/tonne. The OPM for the standalone cement business stood at 29.8% for the quarter, up by 630bp yoy. The cement business's Return on Average Capital Employed (RoACE) stood at 21.1% (20.4%) during the quarter.

Exhibit 1: Cement Realisations (Rs/Tonne) - (Stand-alone)

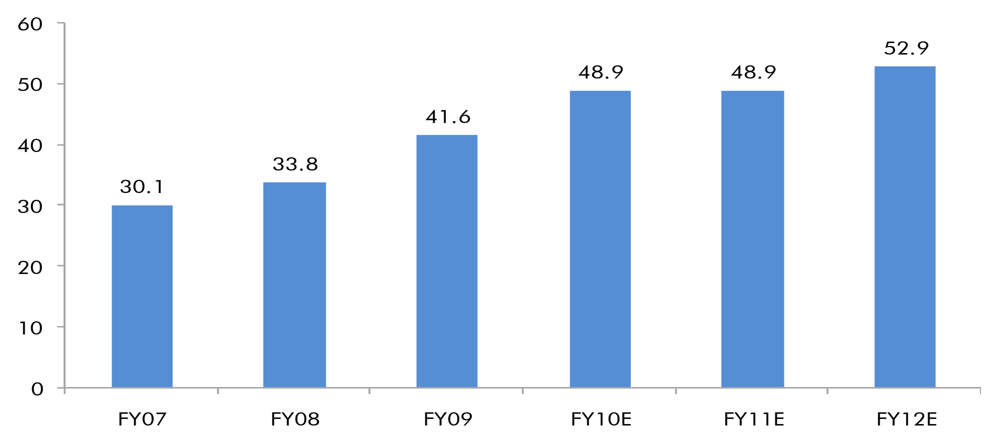


Source: Company, Angel Research

Capacity Expansions on schedule

The 1.55mtpa first unit of the Kotputli plant became operational in January 2010, while the second unit is expected to be commissioned in February 2010. The company's consolidated cement capacity is expected to touch 48.9mtpa by the end of FY2010E. On a consolidated basis, the company expects to incur a total capex of close to Rs3,300cr in FY2010E and FY2011E.

Exhibit 2: Capacity ramp up (mtpa)



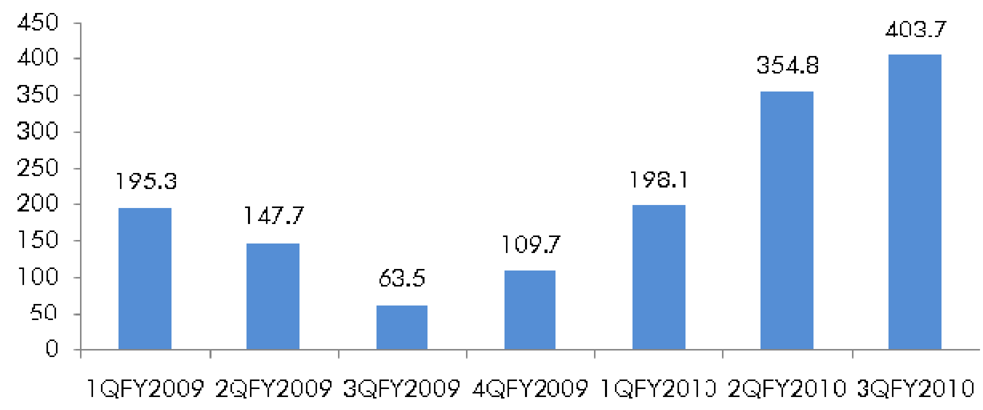
Source: Company, Angel Research

VSF Business: Posts stellar results

The net revenue of the VSF business grew by 71% during the quarter. Further, this division registered the highest-ever quarterly sales volume of 81,300MT, up by 51% yoy. The increase in volume came on account of strong domestic demand, increased consumer spending in the domestic as well as global markets and a lower global availability of cotton. During the quarter, the domestic sales volume of the VSF division was up by 33%, while the export volume was up by 209%. The realisations of the business were also up by 13% yoy to Rs109,600 per tonne. Additionally, the OPM of the VSF business improved substantially to 41.8%, on account of a decline in input costs, better economies of scale and the efficient performance of plants. The Operating Profit of this division grew by a whopping 536% to Rs404cr during 3QFY2010. The VSF business, which had a capacity utilisation of 98%, reported a stupendous RoACE of 87.8% (8.4%) during the quarter.

The company is planning to invest Rs1,000cr towards setting up a new VSF plant with a capacity of 80,000tpa at Vilayat in Gujarat. The land for the project has been obtained and the environment clearance is in place. This plant is expected to be operational in FY2013. The company is also doubling the capacity of its overseas Joint Venture in China to 70,000tpa by March 2010.

Exhibit 3: VSF Business – Operating Profit (Rs cr)



Source: Company, Angel Research

Chemical Business

The net revenue of the Chemical Business declined by 5% yoy to Rs121.3cr during the quarter. The sales of this division declined despite a 12% increase in the sales volume to 61,326MT. The division's OPM declined by 280bp to 23.3%.

Exhibit 4: Segment-wise Revenues (Consolidated)

Rs cr	3QFY10	3QFY09	*yoy %*	9MFY10	9MFY09	*yoy %*
Fibre & Pulp	1,050	623	*68.5*	2,794	2,227	*25.5*
Cement	3,635	3,383	*7.4*	11,308	9,551	*18.4*
Sponge Iron	-	298	*-*	111	850	*(86.9)*
Chemicals	121	128	*(5.5)*	373	400	*(6.8)*
Textiles	84	78	*7.7*	258	247	*4.5*
Others	0.2	151	*(99.9)*	0.7	431	*(99.8)*
Total (Gross)	4,891	4,661	*4.9*	14,845	13,705	8.3

Source: Company, Angel Research

Exhibit 5: 3QFY2010 Performance

Y/E March (Rs cr)	3QFY10	3QFY09	% Chg	9MFY10	9MFY09	% Chg
Net Sales	**4,843.5**	**4,610 .4**	*5.1*	**14,715 .2**	**13,549.2**	**8.6**
Net Raw Material Costs	795.1	901.0	*(11.8)*	2,563	2,866	*(10.6)*
(% of Sales)	*16.4*	*19.5*		*17.4*	*21.2*	
Power & Fuel	911.8	1,099.5	*(17.1)*	2,595	2,843	*(8.7)*
(% of Sales)	*18.8*	*23.8*		*17.6*	*21.0*	
Staff Costs	272.1	266.2	*2.2*	783.49	722.4	*8.5*
(% of Sales)	*5.6*	*5.8*		*5.3*	*5.3*	
Freight & Forwarding	673.4	594.3	*13.3*	1,993	1,698	*17.4*
(% of Sales)	*13.9*	*12.9*		*13.5*	*12.5*	
Other Expenses	751.0	749.3	*0.2*	2,169	2,176	*(0.3)*
(% of Sales)	*15.5*	*16.3*		*14.7*	*16.1*	
Total Expenditure	**3,403**	**3,610**	*(5.7)*	**10,104**	**10,305**	*(2.0)*
Operating Profit	**1,440 .2**	**1,000.1**	*44.0*	**4,611.7**	**3,244 .0**	*42.2*
OPM	*29.7*	*21.7*	*8.04*	*31.3*	*23.9*	*7.40*
Interest	79.4	93.9	*(15.5)*	244.8	235.5	*3.9*
Depreciation	254.7	230.2	*10.7*	737.1	640.6	*15.1*
Other Income	71.2	72.5	*(1.9)*	210.5	207.7	*1.4*
PBT (excl. Extr. Items)	**1,177.3**	**748.6**	*57.3*	**3,840.3**	**2,575.5**	*49.1*
Extr. Income/(Expense)	-	-		336.1	-	
PBT (incl. Extr. Items)	**1,177.3**	**748.6**	*57.3*	**4,176.4**	**2,575.5**	*62.2*
Provision for Taxation	381.4	183.3		1,245.3	655.9	*89.9*
(% of PBT)	*32.4*	*24.5*		*29.8*	*25.5*	
MI & Profits of Associates	80.4	105.8		355.0	301.8	
Reported PAT	**715.5**	**459.6**	*55.7*	**2,576 .1**	**1,617.9**	*59.2*
PATM	*14.8*	*10.0*		*17.5*	*11.9*	
EPS (Rs)	**78.0**	**50.1**		**281.0**	**176.4**	
Adjusted PAT	**715.5**	**459.6**	*55.7*	**2,240 .1**	**1,617.9**	*38.5*

Source: Company, Angel Research

Outlook and Valuation

The total cement capacity in India stood at around 219.2mtpa at the end of FY2009, an increase of 21mtpa yoy. Additionally, the capacity is expected to have been augmented by 30mn tonnes in 9MFY2010. We expect these additional capacities to fully ramp-up over the next 3-4 months, which would eventually exert pressure on cement prices. Overall, we expect the industry to add around 76mn tonnes of capacity through FY2010-12E. Such huge capacity additions would eventually result in an oversupply situation in the market, while demand is not expected to keep pace with the supply. All the frontline states in the southern region, like Andhra Pradesh, Tamil Nadu and Karnataka, are witnessing low demand or a fall therein, which is a cause for concern. Most of the capacities that are being expanded are in the southern region; thus, the industry is witnessing aggressive inter-regional stock movement, which pressurises the pricing power and profitability in other regions as well. In the northern market, the capacity utilisation remained healthy at 99% in December 2009, due to the Commonwealth games-related spending.

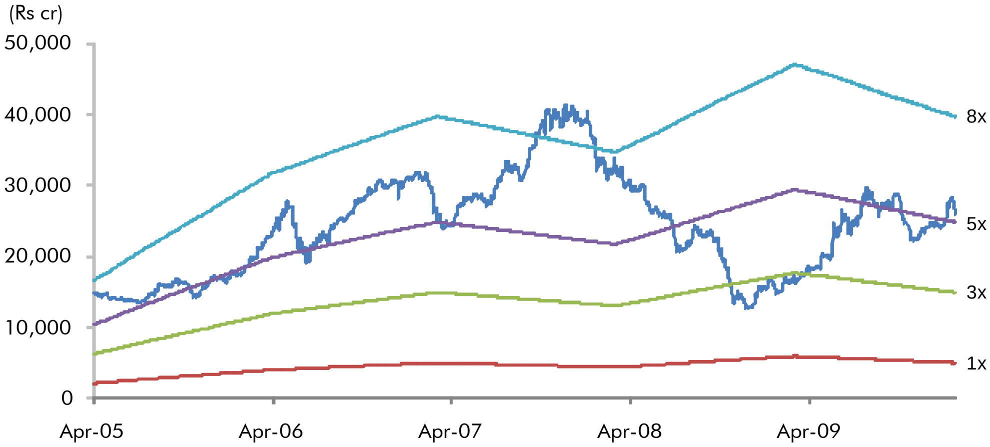
On account of the huge capacity addition, cement prices declined by 2.7% yoy during 3QFY2010. The cement prices rose in the southern and western regions in December, due to distribution constraints, on the back of a shortage in the availability of rail wagons. Further, the instability in the political scenario in Andhra Pradesh resulted in a rebound in the prices in the state, which bottomed out at close to Rs140-145, and also helped in arresting a price fall in other parts of the region. The prices in the northern region were ruling higher in December, on account of the demand arising from the Commonwealth Games. However, the rise in prices is expected to be a short-term trend, as the new capacity addition over the last few months is expected to exert pressure, going ahead. We expect north-based players to do well as compared to south-based players, on account of relatively balanced demand-supply dynamics.

We have derived the value of Grasim on an SOTP basis. We have valued the company's 60.3% stake in Ultratech (post demerger of Samruddhi) at an average of an EV/tonne of US $105/Tonne and an EV/EBITDA of 6.5x FY2012E, after providing a 15% holding company discount to arrive at a value of Rs1,670/share. We have arrived at a value of Rs623/share for Grasim shareholder's direct holding in Ultratech (post demerger). We have valued the VSF business at 5x EV/EBITDA, implying a P/BV of 1.75x on an FY2012E basis. We have assigned the valuation multiple based on the VSF business's superior RoCE as compared to its global peers (which are trading at 3x P/BV, based on the CY2012E book value). **Hence, our SOTP Fair Value for Grasim works out to Rs2,861. We upgrade the stock to Accumulate from Neutral.**

Exhibit 6: SOTP Valuation for Grasim

Segments	Valuation Parameter	Per Share (Rs)
Grasim's stake in Ultratech (@ 15% holding company discount) (60.3%)	Average of EV/Tonne @US$105/Tonne, EV/EBITDA of 6.5x FY2012E	1,670
Grasim shareholder's holding in Ultratech (19.1%)	Average of EV/Tonne @US$105/Tonne, EV/EBITDA of 6.5x FY2012E	623
VSF	EV/EBITDA of 5x FY2012E	421
Chemicals and Others	EV/EBITDA of 5x FY2012E	44
Cash and Unquoted Investments	P/BV of 1x FY2012E	103
Per share value		2,861

Exhibit 7: 1-year forward P/B band



Source: Company, Angel Research

Research Team Tel: 022-4040 3800 E-mail: research@angeltrade.com Website: www.angeltrade.com

DISCLAIMER

Note: Please refer important `Stock Holding Disclosure' report on Angel web-site (Research Section).

Disclosure of Interest Statement	Grasim
1. Analyst ownership of the stock	No
2. Angel Group ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below Rs 5 lakh for Angel, its Group companies and Directors.

Ratings (Returns) :	Buy (> 15%) Reduce (-5% to -15%)	Accumulate (5% to 15%) Sell (< -15%)	Neutral (-5 to 5%)

Address: Acme Plaza, 'A' Wing, 3rd Floor, M.V. Road, Opp. Sangam Cinema, Andheri (E), Mumbai - 400 059.
Tel : (022) 3952 4568 / 4040 3800

Angel Broking Ltd: BSE Sebi Regn No : INB 010996539 / CDSL Regn No: IN - DP - CDSL - 234 - 2004 / PMS Regn Code: PM/INP000001546 Angel Securities Ltd:BSE: INB010994639/INF010994639 NSE: INB230994635/INF230994635 Membership numbers: BSE 028/NSE:09946

Angel Capital & Debt Market Ltd: INB 231279838 / NSE FNO: INF 231279838 / NSE Member code -12798 Angel Commodities Broking (P) Ltd: MCX Member ID: 12685 / FMC Regn No: MCX / TCM / CORP / 0037 NCDEX : Member ID 00220 / FMC Regn No: NCDEX / TCM / CORP / 0302