IL&FS INVESTSMART
Institutional Equity

Cement

Grasim Industries

Vishal Mishra
+91 22 67069943
vishal.mishra@investsmartindia.com

Shareholding (%)

Promoters	*25.2*
FII's	*23.0*
MFs	*7.9*
Insurance Co.	*12.8*
Others	*31.1*

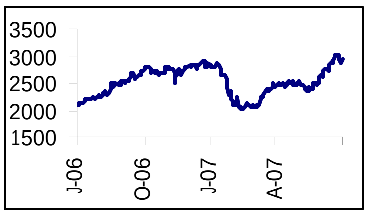
Share price performance

52-week high/low (Rs) 3060/1932

	-1m	-3m	-12m
Abs (%)	11.7	20.3	41.6
Rel* (%)	8.9	11.7	0.3

*to Nifty

Stock chart



Robust performance across segments leads to good results

Robust performance across business segments enabled Grasim Industries (Grasim) to report an impressive 29.2% YoY growth in Q1FY08. Higher realizations and volumes from the cement and VSF divisions supported this robust YoY growth during the quarter. Operating margins for the quarter stood at 32.4%, a growth of 525bps YoY.

At the current price, the stock is trading at a P/E of 16x and an EV/EBIDTA of 10.9x FY08E. In the cement division, Grasim is operating at almost full capacity. The margins in the VSF division are expected to come under pressure, going forward, in view of the expected softening of VSF prices and the rising costs of pulp and sulphur. Moreover, ECU realizations in the chemicals business are also expected to remain under pressure during FY08E. The performance of sponge iron division would improve only after the availability of gas improves (expected by Mar-2008). Given these constraining factors, we maintain an 'Accumulate' rating on the stock.

- **Cement division's margins expand on firm prices:** During Q1FY08, the topline of Grasim's cement division grew by 21.2% YoY to Rs 14.1 bn. Firm cement prices translated into a 13.1% increase in grey cement realizations at Rs 3,083 per tonne; volumes were also higher by 11.4% to 3.9mn tonnes. The RMC and white cement businesses grew by 19% and 8% respectively, supported by higher volumes. Buoyed by higher cement prices, the operating profit margins of the cement division expanded by 140 bps YoY to 35.3%. The margins expansion would have been higher but for a 28% increase in fuel costs (due to higher pet coke prices and lower availability of coal through linkages) and an 8% increase in freight costs.

Table 1. Cement division

(Rs mn)	Q1FY08	Q1FY07	Change
Net sales	13,907	11,100	25.3%
PBDIT	4,911	3,765	30.4%
PBDIT margins	35.3%	33.9%	

Source: IISL research, company

- **Higher volumes drive VSF division growth:** Grasim's VSF division continued its strong performance during the quarter, marked by a revenue growth of 58.6% YoY. With the plant now operating at 102%, the company reported a 52% growth in production. It is to be noted here that the production was imapcted in Q1FY07 due to water shortage. VSF sales volumes were thus up 34%. Buoyed by strong

Accumulate

Rs2945

30 July 2007

Market cap
Rs bn 270
US$ bn 7

Avg 3m daily volume
153,380

Avg 3m daily value
USD mn 10

Shares outstanding (mn)
92

Reuters
GRAS.BO/GRASIM.NS

Bloomberg
GRASIM IN

Sensex
15,261

Nifty
4,440

Grasim Industries

global demand, realizations too were up 20% YoY. On the cost front, the rising global pulp prices remains a concern for the industry; the impact of the same on Grasim, however, was muted due to rupee appreciation and because the company met part of its requirements captively. Operating profit margins thus improved from 26 % in Q1FY07 to 36.6% in Q1FY08.

Table 2. VSF division

(Rs mn)	Q1FY08	Q1FY07	Change
Net sales	6,999	4,397	59.2%
PBDIT	2,563	1,143	124.2%
PBDIT margins	36.6%	26.0%	

Source: IISL research, company

- Sponge iron division turns around: In the past, the performance of Grasim's sponge iron business had been marred by the limited availability of gas. However, the use of alternative fuels has improved production. In line with the increase in global scrap prices, domestic sponge iron prices had seen a sharp increase during the quarter. Consequently, the company reported a 24.8% growth in net sales of this division, with realizations increasing 22%. While an increase in the feedstock did have a bearing on the overall cost of production, the same was more than offset by the increase in realizations; this resulted in a 790 bps improvement in operating profit margins to 16.1%.

Table 3. Sponge iron division

(Rs mn)	Q1FY08	Q1FY07	Change
Net sales	2,188	1,753	24.8%
PBDIT	353	144	145.1%
PBDIT margins	16.1%	8.2%	

Source: IISL research, company

- Chemical division recovers, however, ECU realizations remain under pressure: In the past, water shortage has impacted the performance of Grasim's ECU division. However, with this issue now resolved, the division reported a 39% increase in the production of caustic soda; consequently, sales of caustic soda sales were higher by 40%. ECU realizations, however, declined by 10% YoY to Rs 17,254 per tonne due to steep fall in chorine and hydro choric acid coupled with stable caustic soda prices. Despite the same, the division reported a 740 bps improvement in operating profit margins to 32.6%. The company has converted its plant to a membrane cell plant, reducing its power costs.

Table 4. Chemicals division

(Rs mn)	Q1FY08	Q1FY07	Change
Net sales	863	710	21.5%
PBDIT	281	179	57.0%
PBDIT margins	32.6%	25.2%	

Source: IISL research, company

Grasim Industries

- Large capex plans over next two years: Over the next two years, Grasim intends to embark on an aggressive expansion plan by incurring a capex of Rs 49.4 bn. Of this, the company is likely to incur Rs 40.9 bn for increasing the capacity of its cement division by 8.8mn tonne; this includes setting up a 96MW thermal power plant, two 75MW thermal power plants, a 1.3mn tonne grinding unit, 27 RMC plants with a capacity of 6.2mn cu. mtrs. For the VSF division, Grasim has set aside Rs 6.9 bn for the modernization and expansion of its Kharach plant to 63,875 TPA. The balance is likely to be utilised for expansions in its chemical, textile and other divisions.
- Valuations: At the current price, the stock is trading at a P/E of 16x and an EV/EBIDTA of 10.9x FY08E. Grasim is operating at almost full capacity in the cement division. The margins in the VSF division are expected to come under pressure, going forward, in view of the expected softening of VSF prices and the rising costs of pulp and sulphur. Moreover, ECU realizations in the chemicals business are also expected to remain under pressure during FY08E. The performance of the sponge iron division would improve only after the availability of gas improves (expected by Mar-2008). Given these constraining factors, we maintain an 'Accumulate' rating on the stock.

Table 2. Quarterly result table

Rs mn	Q1FY08	Q1FY07	YoY (%)	Q4FY07	QoQ (%)
Net Sales	24,447.9	18,917.3	29.2	24,937.5	(2.0)
Total Expenses	16,526.6	13,782.0	19.9	17,995.2	(8.2)
EBIDTA	7,921.3	5,135.3	54.3	6,942.3	14.1
EBIDTA %	32.4%	27.1%		27.8%	
Other Income	677.4	374.7	80.8	775.8	(12.7)
Interest	284.7	237.6	19.8	366.3	(22.3)
Depreciation	850.0	740.9	14.7	875.6	(2.9)
PBT	7,464.0	4,531.5	64.7	6,476.2	15.3
EO Items	-	-		371.0	
Tax	2,347.4	1,412.5	66.2	2,102.3	11.7
Net Profit	5,116.6	3,119.0	64.0	4,744.9	7.8
Adj Net Profit	5,116.6	3,119.0	64.0	4,744.9	7.8
Adj EPS	55.8	34.0	64.0	51.7	7.8

Source: IISL research, company

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