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Orient Paper & Industries Ltd

Demerger to trigger value unlocking process

Result Update

July 28, 2011

Reco	**Previous Reco**
Buy	Buy
CMP	**Target Price**
Rs 62	Rs82

EPS change FY12E/13E (%)	NA
Target Price change (%)	+11
Nifty	5,547
Sensex	18,432

Price Performance

(%)	1M	3M	6M	12M
Absolute	9	7	21	15
Rel. to Nifty	8	13	24	13

Source: Bloomberg

Relative Price Chart

Source: Bloomberg

Stock Details

Sector	Cement
Bloomberg	OPI@IN
Equity Capital (Rs mn)	193
Face Value(Rs)	1
No of shares o/s (mn)	193
52 Week H/L	69/45
Market Cap (Rs bn/USD mn)	12/272
Daily Avg Volume (No of sh)	51081
Daily Avg Turnover (US$mn)	0.1

Shareholding Pattern (%)

	Jun-11	Mar-11	Dec-10
Promoters	33.6	33.6	33.6
FII/NRI	4.7	3.8	3.9
Institutions	36.0	34.5	34.1
Private Corp	13.3	14.6	14.6
Public	12.4	13.5	13.7

Source: Capitaline

Ajit Motwani
ajit.motwani@emkayglobal.com
+91 22 6612 1255

Chandan Asrani
chandan.asrani@emkayglobal.com
+91 22 6612 1241

- Q1 APAT at Rs584mn (+70% yoy) above est (Rs457mn) led Revenues at Rs5.33bn (+21%), Cement (+11.4%), Electricals (+22.3%) & Paper (+137%)
- Cement revenues +11.4% yoy to Rs3.34 bn as realizations improved 29% yoy and 5.6% qoq –driven by elevated levels of FY11 exit cement prices resulting in higher quarter averages
- Board approves de-merger of cement business into a new wholly owned sub- Orient Cement Ltd (OCL) - triggers the much awaited value unlocking process
- Stock trades at undemanding valuation of 6.6x FY12 PER & EV/EBIDTA of 4X. We maintain our BUY rating on the stock with revised target price of Rs82

Higher than expected realizations boost cement revenues…

Q1FY12 revenues grew 21% yoy to Rs5.33bn (estimates-Rs5.1bn) led by better than expected cement realization. Cement revenues grew 11.4% yoy driven by a sharp 29.4% yoy jump in cement realizations to Rs3565/t even volumes declined 14% yoy due to decline in cement demand in AP. Cement realization came in better than expected as higher FY11 exit prices sustained till mid-May resulting in higher average prices for the quarter. Electrical division registered healthy topline with growth of 22.3% yoy.

… driving better than expected EBIDTA growth of 54.6%

With better than expected realization, Q1FY12 EBIDTA came in at Rs1.1 bn +54.6%yoy, above estimates (Rs0.94 bn). Overall EBIDTA margins at 20.8% improved by 453bps yoy driven by 450 bps improvement in EBIT margins of Cement division to 31.8% Cement EBIT/t stood at Rs1133, +51% yoy. With 8% decline in interest charge, OPIL's APAT at Rs584 mn came in above estimates of Rs457 mn, a growth of 70% yoy. Reported net profit includes Rs85.5 mn of income from sale of CERs and Rs75 mn of one-time stores write off (for paper division).

Board approves de-merger of cement business - triggers value unlocking process

The Board has approved De-merger of Cement Business into a new wholly owned sub- Orient Cement Ltd (OCL). Post the necessary approval, OPIL shareholder will get 1 share of OCL for each share held in OPIL. Hence OCL will have mirror shareholding of OPIL. Effective date of demerger is 1st April-12. The de-merger creates focused cement play for OPIL shareholder and triggers the much awaited value unlocking process, apart from providing separate platform for each businesses to pursue growth opportunities.

Maintain BUY with price target price of Rs82

Though sustainability of recent levels of cement prices remain uncertain, we believe that OPIL's least cost of production will help the company to see it through this cyclical downturn. Stock trades at 6.6x FY12 PER & EV/EBIDTA of 4X. Maintain BUY. Upgrade TP to Rs82 as we now value cement business at EV/t of USD70 as compared to USD60 earlier. We expect the re-rating OPIL's cement business as the de-merger will ensure that the cement cash flows will be dedicatedly used for funding the growth of the business rather than supporting the losses of the paper division.

Key Financials Rs mn

YE-Mar	Net Sales	EBITDA (Core)	(%)	APAT	EPS (Rs)	EPS % chg	RoE (%)	P/E	EV/ EBITDA	P/BV
FY10	16,198	3,074	19.0	1,593	8.3	-35.9	22.7	7.5	5.3	1.6
FY11P	19,590	2,951	15.1	1,431	7.4	-10.2	17.2	8.3	5.5	1.3
FY12E	24,740	3,868	15.6	1,800	9.3	25.8	18.5	6.6	4.0	1.1
FY13E	28,756	4,558	15.9	2,186	11.3	21.5	19.0	5.5	3.1	1.0

Result Table

Rs mn	Q1FY11	Q2FY11	Q3FY11	Q4FY11	Q1FY12E	YoY (%)	QoQ (%)	YTD'12	YTD'11	YoY (%)
Revenue	**4,416**	**3,829**	**4,384**	**6,961**	**5,339**	20.9	-23.3	**5,339**	**4,416**	20.9
Expenditure	**3,698**	**3,641**	**3,643**	**5,656**	**4,230**	14.4	-25.2	**4,230**	**3,698**	14.4
as % of sales	*84%*	*95%*	*83%*	*81%*	*79%*			*79%*	*84%*	
Raw Material Consumed	1,472	1,472	1,637	2,418	2,063	40.1	-14.7	2,063	1,472	40.1
as % of sales	*33%*	*38%*	*37%*	*35%*	*39%*			*39%*	*33%*	
Stock Adjustments	-29	-84	-396	549	-400	1264.1	-172.8	-400	-29	1264.1
as % of sales	*-1%*	*-2%*	*-9%*	*8%*	*-7%*			*-7%*	*-1%*	
Consumption of Stores	65	176	182	186	139	113.7	-25.4	139	65	113.7
as % of sales	*1%*	*5%*	*4%*	*3%*	*3%*			*3%*	*1%*	
Power, Oil & Fuel	837	802	816	845	850	1.6	0.6	850	837	1.6
as % of sales	*19%*	*21%*	*19%*	*12%*	*16%*			*16%*	*19%*	
Employee Expenses	279	287	302	322	352	25.9	9.1	352	279	25.9
as % of sales	*6%*	*8%*	*7%*	*5%*	*7%*			*7%*	*6%*	
Freight and selling exp	639	503	598	828	729	14.0	-12.0	729	639	14.0
as % of sales	*14%*	*13%*	*14%*	*12%*	*14%*			*14%*	*14%*	
Provisions & Write Offs	-	-	-	-	(75)			(75)	-	
as % of sales	*0%*	*0%*	*0%*	*0%*	*-1%*			*-1%*	*0%*	
Other Expenses	436	484	503	508	573	31.5	12.9	573	436	31.5
as % of sales	*10%*	*13%*	*11%*	*7%*	*11%*			*11%*	*10%*	
EBITDA	**718**	**188**	**741**	**1,304**	**1,109**	54.6	-14.9	**1,109**	**718**	54.6
Depreciation	192	200	208	215	213	11.1	-0.9	213	192	11.1
EBIT	**526**	**-12**	**534**	**1,089**	**896**	70.4	-17.7	**896**	**526**	70.4
Other Income	88	98	36	155	60	-31.3	-61.2	60	88	-31.3
Interest	101	76	107	134	93	-7.7	-30.5	93	101	-7.7
PBT	**513**	**9**	**462**	**1,111**	**864**	68.4	-22.3	**864**	**513**	68.4
Total Tax	171	4	153	336	280	64.2	-16.8	280	171	64.2
Adjusted PAT	**342**	**5**	**309**	**775**	**584**	70.5	-24.6	**584**	**342**	70.5
Extra ordinary items					10			10		
Reported PAT	**342**	**5**	**309**	**775**	**594**	73.4	-23.4	**594**	**342**	73.4
(Profit)/loss from JV's/Ass/MI										
PAT after MI	**342**	**5**	**309**	**775**	**594**	73.4	-23.4	**594**	**342**	73.4
Reported EPS	**1.8**	**0.0**	**1.6**	**4.0**	**3.0**	70.5	-24.6	**3.03**	**1.78**	70.5

Margins (%)						**bps**	**bps**			**bps**
EBIDTA	16.3	4.9	16.9	18.7	20.8	453	204	20.8	16.3	453
EBIT	0.0	0.0	0.0	0.0	0.0	0	0	0.0	0.0	0
EBT	11.6	0.2	10.5	16.0	16.2	456	21	16.2	11.6	456
PAT	7.8	0.1	7.0	11.1	10.9	318	-20	10.9	7.8	318
Effective Tax rate	33.2	46.2	33.1	30.3	32.4	-83	214	32.4	33.2	-83

Segmental Results

	Q1FY11	Q2FY11	Q3FY11	Q4FY11	Q1FY12E	YoY (%)	QoQ (%)	YTD'12	YTD'11	YoY (%)
Revenue										
Paper & Board	214	691	891	977	508	136.8	-48.1	508	214	136.8
Cement	2843	1861	2286	3342	3167	11.4	-5.3	3167	2843	11.4
Electric Fans	1347	1264	1189	2622	1649	22.3	-37.1	1649	1347	22.3
EBIT										
Paper & Board	-233	-34	24	-94	-154	-34.0	64.1	-154	-233	-34.0
Cement	775	54	466	1036	1007	29.9	-2.8	1007	775	29.9
Electric Fans	96	66	100	309	121	26.0	-61.0	121	96	26.0
EBIT margin						bps	bps			bps
Paper & Board	-108.8	-4.9	2.7	-9.6	-30.3	7848	-2071	-30.3	-108.8	7848
Cement	27.3	2.9	20.4	31.0	31.8	453	80	31.8	27.3	453
Electric Fans	7.1	5.2	8.4	11.8	7.3	21	-447	7.3	7.1	21

Segmental performance

Cement

Revenues from cement segment grew 11.4% yoy to Rs3.17 bn led by 29.4% improvement in realizations effect of elevated cement exit prices for FY11 continued till Mid May taking average quarter realizations higher. Volumes at 0.88 mnt declined 13.9% yoy and 10.3% sequentially. Total cost per tonne at Rs2431, up 21.3% yoy, came in lower than estimated. Consequently EBIT per tonne surprised positively at Rs1133, up 51% yoy.

OPIL to set up 3mtpa Greenfield cement plant at Karnataka – capex of Rs17.2 bn

In its second phase of capacity expansion OPIL plans to set up 3 mtpa Greenfield cement plant at Gulburga, Karnataka along with a 50 MW power plant .The total project cost is ~ Rs17.2 bn which would be funded by internal accruals and a debt of Rs4-5bn. Land acquisition for the plant is currently on and equipment order are expected to be placed by Q3FY12. The plant is expected to be completed by end FY15 or early FY16.

Paper division

Revenues from paper division at Rs508 mn, up 136.8% yoy were better than estimates of Rs350mn. However, the segment continued to disappoint and reported loss of Rs229mn (Loss of Rs217 mn from the Amalai Plant).

However the company plans to direct focused efforts towards the turnaround of this segment. It plans to set up a 55 MW power plant to improve the cost efficiencies of the paper plant. This plant is at an advanced stage of completion and is expected to be operational by Q1FY12.Also it has also implemented modern technologies to reduce the water consumption by 25% and constructed 2 large water reservoirs with a capacity of 250 mn gallons which would help the company to increase production days by 60.

Electrical Division

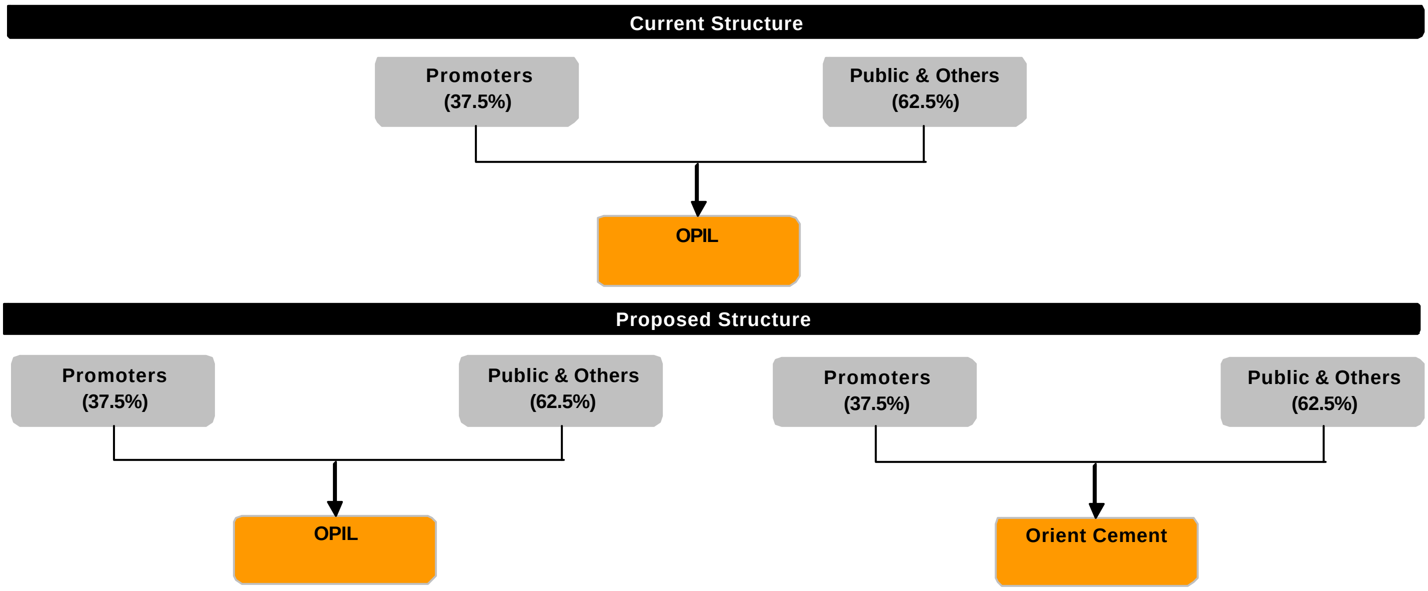
Electricals division continued its impressive topline performance with revenues of Rs1.65 bn (+22.3% yoy). However EBIT at Rs121mn (+26%yoy) came in lower than estimates of Rs168mn. Margins almost remained flat at 7.3% (+20bps yoy). The company plans to further diversify the range of its consumer electrical products by addition of household appliances such as Mixers, Geysers, Coolers, and Room Heaters in addition to fans and lighting products, which we believe will boost its revenue growth, given its experience in electrical division and established distribution networks.

Board approves de-merger of cement business - triggers the much awaited value unlocking process

The board of directors of OPIL approved a proposal to demerge the cement business of OPIL into Orient Cement Limited by way of a classical demerger with mirror shareholding. The demerger is subject to approval of Hon'ble High Court of Orissa, shareholders and creditors of OPIL, SEBI and stock exchanges.

Orient Cement Limited will constitute the cement business of OPIL. OPIL will continue to carry on the non cement business (paper and electricals and other investments). The Shareholders of OPIL will get one new equity share of Orient Cement for each equity share that they hold in OPIL, in addition to their existing OPIL shares. Hence OCL will have mirror shareholding of OPIL. Effective date of demerger is 1st April 2012. Orient cement limited is proposed to be listed on BSE and NSE. The Demerger Creates pure play cement company that triggers the much awaited value unlocking process, apart from providing separate platform for each businesses to explore various options to augment their growth plans.

Shareholding Structure Pre & Post De-merger



Note: Promoter holding calculated post assuming conversion of preferential warrants

Maintain BUY with revised price target price of Rs82

Though sustainability of recent levels of cement prices remain uncertain, we believe that OPIL's least cost of production will help the company to see it through this cyclical downturn. However we believe that the restructuring of business could kick start the long awaited value-unlocking process and support stock performance. Stock trades at undemanding valuation of 6.6x FY12 PER & EV/EBIDTA of 4X. Upgrade target price to Rs82 as we now value cement business at EV/t of USD70 as compared to USD60 earlier. We expect the market to re-rate OPIL's cement business as the de-merger will ensure that the cement cash flow will be dedicatedly used for funding the growth of the business rather than supporting the losses of the paper division.

SOTP valuation

Replacement Cost Workings	Valuation Measure	Value (Rs mn)
Cement EV	Values at 30% discount to replacement cost of USD 100/ton	15750
Target Cement EV/Tonne		70
Add		
Paper	0.25X FY12E sales	914
Electrical Consumer Durable	3X FY12E EV/EBIDTA	2334
Value Of investments	@ 50% discount to CMP	447
Target EV		19445
Less:		
Net Debt	FY12	3550
Target Mcap		15895
Equity Shares in issue		193
Fair Value		**82**

Key Financials

Income Statement

Y/E, Mar (Rs. m)	FY10	FY11P	FY12E	FY13E
Net Sales	**16,198**	**19,590**	**24,740**	**28,756**
Growth (%)	7.8	20.9	26.3	16.2
Expenditure	**13,124**	**16,639**	**20,872**	**24,198**
Materials Consumed	5,642	6,879	8,808	10,439
Construction Exp	4,566	6,112	7,780	9,005
Employee Cost	1,040	1,174	1,327	1,433
Other Exp	1,876	2,473	2,957	3,321
EBITDA	**3,074**	**2,951**	**3,868**	**4,558**
Growth (%)	(21.5)	(4.0)	31.1	17.8
EBITDA margin (%)	19.0	15.1	15.6	15.9
Depreciation	550	815	890	1,012
EBIT	2,524	2,136	2,978	3,546
EBIT margin (%)	15.6	10.9	12.0	12.3
Other Income	163	377	240	240
Interest expenses	345	418	571	571
PBT	**2,341**	**2,095**	**2,647**	**3,215**
Tax	748	664	847	1,029
Effective tax rate (%)	31.9	31.7	32.0	32.0
Adjusted PAT	**1,593**	**1,431**	**1,800**	**2,186**
Growth (%)	(35.9)	(10.2)	25.8	21.5
Net Margin (%)	9.8	7.3	7.3	7.6
(Profit)/loss from JV's/Ass/MI				
Adj. PAT After JVs/Ass/MI	**1,593**	**1,431**	**1,800**	**2,186**
E/O items	0	0	0	0
Reported PAT	**1,593**	**1,431**	**1,800**	**2,186**
Growth (%)	*-20.4*	*-10.2*	*25.8*	*21.5*

Balance Sheet

Y/E, Mar (Rs. m)	FY10	FY11P	FY12E	FY13E
Equity share capital	193	365	365	365
Reserves & surplus	7,561	8,652	10,235	12,204
Shareholders Funds	**7,754**	**9,017**	**10,599**	**12,568**
Secured Loans	4,171	3,974	3,974	3,974
Unsecured Loans	964	1,466	1,466	1,466
Loan Funds	**5,135**	**5,440**	**5,440**	**5,440**
Net Deferred Taxes	1103	1354	1354	1354
Total Liabilities	**15,132**	**17,193**	**18,776**	**20,745**
Gross Block	16,365	17,919	18,169	20,519
Less: Acc Depreciation	5,206	5,963	6,853	7,865
Net block	**11,159**	**11,955**	**11,315**	**12,653**
Capital WIP	568	657	2,137	1,473
Investment	**471**	**663**	**663**	**663**
Current Assets	**4,888**	**6,030**	**7,514**	**9,380**
Inventories	1,503	1,642	2,074	2,411
Sundry Debtors	1,844	2,398	2,711	3,151
Cash and Bank	464	588	1,327	2,417
Loans and Advances	1,077	1,401	1,401	1,401
Other current assets	96	36	68	79
Current Liab & Prov	3,153	3,503	4,275	4,858
Current liabilities	2,346	2,821	3,592	4,176
Provisions	807	683	683	683
Net current assets	**1,735**	**2,527**	**3,239**	**4,522**
Miscellaneous Exps	0	0	0	0
Total Assets	**15,132**	**17,193**	**18,775**	**20,744**

Cash Flow

Y/E, Mar (Rs. m)	FY10	FY11P	FY12E	FY13E
PBT (Ex-Other income)	**2341**	**2095**	**2407**	**2975**
Depreciation	550	815	890	1012
Interest Provided	345	418	571	571
Other Non-Cash items	-33	-42	0	0
Chg in working cap	-137	-378	-4	-205
Tax paid	-448	-564	-847	-1029
Operating Cashflow	**2619**	**2344**	**3017**	**3325**
Capital expenditure	-1916	-1782	-1730	-1687
Free Cash Flow	**703**	**562**	**1287**	**1638**
Other income	62	59	240	240
Investments	-380	-193	0	0
Investing Cashflow	**-2234**	**-1916**	**-1490**	**-1447**
Equity Capital Raised	4	172	0	0
Loans Taken / (Repaid)	512	304	0	0
Interest Paid	-434	-448	-571	-571
Dividend paid (incl tax)	-338	-336	-218	-218
Income from investments	0	0	0	0
Others	2	3	0	0
Financing Cashflow	**-254**	**-304**	**-789**	**-789**
Net chg in cash	**131**	**124**	**739**	**1090**
Opening cash position	333	464	588	1327
Closing cash position	**464**	**588**	**1327**	**2417**

Key Ratios

Y/E, Mar	FY10	FY11P	FY12E	FY13E
Profitability (%)				
EBITDA Margin	19.0	15.1	15.6	15.9
Net Margin	9.8	7.3	7.3	7.6
ROCE	21.1	16.9	19.5	20.7
ROE	22.7	17.2	18.5	19.0
RoIC	29.7	16.3	22.0	25.4
Per Share Data (Rs)				
EPS	8.3	7.4	9.3	11.3
CEPS	11.1	11.6	13.9	16.6
BVPS	39.7	46.3	54.5	64.7
DPS	1.5	1.5	1.0	1.0
Valuations (x)				
PER	7.5	8.3	6.6	5.5
P/CEPS	5.6	5.3	4.4	3.7
P/BV	1.6	1.3	1.1	1.0
EV / Sales	1.0	0.8	0.6	0.5
EV / EBITDA	5.3	5.5	4.0	3.1
Dividend Yield (%)	2.4	2.4	1.6	1.6
Gearing Ratio (x)				
Net Debt/ Equity	0.6	0.5	0.4	0.2
Net Debt/EBIDTA	1.5	1.7	1.1	0.7
Working Cap Cycle (days)	23.0	20.0	27.3	12.4

Recommendation History: Orient Paper & Industries – OPI IN

Date	Reports	Reco	CMP	Target
28/04/2011	Orient Paper Q4FY11 Result Update	Buy	60	74
21/01/2011	Orient Paper Q3FY11 Result Update	Buy	50	77
16/11/2010	Orient Paper Q2FY11 Result Update	Buy	65	77
30/07/2010	Orient Paper Q1FY11 Result Update	Buy	54	63

Recent Research Reports

Date	Reports	Reco	CMP	Target
22/07/2011	Century Plyboards Q1FY12 Result Update	Buy	72	84
13/06/2011	Cement Sector Update			
13/06/2011	ILFS Transportation Management Meet Update	Accumulate	207	243
02/06/2011	Cement Sector Update			

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